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ABSTRACT

Organized in two parts, this book explores methods for incorporating concern for human needs into economic policies in eastern and central European countries that are making the transition to a market economy. Part I of the book considers economic reform, social policy, and child welfare in central and eastern Europe as a whole. Topics include: (1) child welfare, and social policy trends and alternatives, before and after the economic reform; (2) the efficiency, cost, and underlying philosophy of the models of social policy in the United States, Germany, and Sweden; and (3) the components and implementation of economic reforms and the consequences of these reforms for child and human welfare. Part II of the book profiles four case studies of efforts to reform social policies for children in central and eastern Europe. These studies include analyses of reforms in Hungary and Poland that have been underway for some time, and reforms in Bulgaria and Czechoslovakia that were introduced in 1991. A reference list of more than 200 items, an author index, and a subject index are provided. (BC)

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Safety Nets and Social Policies in Central and Eastern Europe

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Children and the Transition to the Market Economy

Safety Nets and Social Policies in Central and Eastern Europe

Edited by

Giovanni Andrea Cornia and Sándor Sipos

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Avebury

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Abbreviations

AFDC	Aid to families with dependent children
CEE	Central and eastern Europe: Bulgaria, Czech and Slovak Federal Republic, Hungary, Poland, Romania, Soviet Union, Yugoslavia
CETA	Comprehensive Employment and Training Act
CMEA	Council of Mutual Economic Assistance
CPI	Consumer price index
CSFR	Czech and Slovak Federal Republic
GDP	Gross domestic product
GDR	German Democratic Republic
GMP	Gross Material product
Goskomstat	State Commission on Statistics of the Soviet Union
ICDC	International Child Development Centre
ILO	International Labour Organisation
IMF	International Monetary Fund
IMR	Infant mortality rate
ISSA	International Social Security Association
LIS	Luxembourg Income Study
NMP	Net material product
OASDI	Old-age, survivor and disability insurance
OECD	Organization for Economic Co-operation and Development
U5MR	Under-5 mortality rate
UNDP	United Nations Development Programme
UNICEF	United Nations Children's Fund
USA	United States of America
USSR	Union of Soviet Socialist Republics
WHO	World Health Organization

Definitions

Absolute poverty line: The income level which allows for the least costly satisfaction of a minimum nutritionally adequate diet plus a few other essential non-food requirements.

Child poverty rate: Percentage of children living in poor families. Poor children may suffer various deprivations which may retard their physical, cognitive and social development.

Child and family policy: The set of measures and provisions focusing on the children and their families. Usually involves transfers and public expenditures in support of children and families.

Distribution according to work: Theoretical principle guiding distribution during socialism. According to this principle everyone in society is entitled to a share of goods in proportion to his/her labour contribution. Exploitation and other factor incomes than labour are excluded.

GDP (Gross domestic product): The total final output of goods and services produced by an economy — that is by residents and non-residents, regardless of the allocation to domestic and foreign claims. It is calculated without making deductions for depreciation.

GMP (Gross material product): The total final output of goods and 'productive' services produced by an economy. It includes depreciation but disregards 'non-productive' activities such as health care, education, culture, administration, etc.

IMR (Infant mortality rate): Annual deaths of infants under one year of age per 1,000 live births. More specifically, this is the probability of dying between birth and one year of age.

Low Birth Weight: The percentage of births below 2,500 g, which is a sensitive measure of mother's health and nutrition during pregnancy and before. The lower an infant's birth weight below 2,500 g, the greater the infant's vulnerability to infections and other problems and the greater the risk of sickness and death.

Maternal mortality: Annual number of deaths of women from pregnancy-related causes per 100,000 live births.

Means-tested benefits: Benefits granted to people if their assessed income does not exceed a given income threshold (which is normally fairly low). Usually these benefits are targeted to the needy. Their finance falls exclusively on public revenues.

NMP (Net material product): Total final output of goods and productive services produced by an economy. NMP does not include depreciation and disregards certain services as 'non-productive' activities (i.e., health care, education, culture, administration, etc.).

Party-State socialism: Form of government which concentrates power in the hand of the ruling communist party and provides only token representation for various social groups. Usually involves the dominance of state or other 'socialist' form of ownership and excessive control of the economy and society.

Relative poverty line: The income level which allows the satisfaction of minimum socially accepted needs. In industrialized countries, the relative poverty line is generally higher than abstract poverty line. People living in relative poverty suffer certain deprivations compared to non-poor members of the society. Relative poverty lines are usually expressed as being between 40 or 50 per cent of average or median income.

Safety nets: Series of public (and private) measures which aim to prevent the massive impoverishment of the population. Includes measures ensuring minimum family income through the establishment of minimum wages and pension benefits, unemployment compensation and means-tested social assistance benefits. It also includes the direct provision of essential services and in extreme cases rationing shelters, etc.

Shock therapy: An extreme version of stabilization and institutional reforms. Measures include very radical and sudden changes in budget deficit, monetary policy, elimination of subsidies, devaluation, trade and currency liberalization all at once.

Shortageflation: Dual manifestation of inflation through price increases associated with shortages of goods in the market.

Shortage economy: An economy in which soft budget constraints result in over-demand and consequent shortages. Economic actors react to shortages by increasing their stocks which, in turn, perpetuates shortages and dual simultaneous manifestation of inflation through price increases associated with shortages of goods in the market.

Social policy: Set of measures which aim to achieve a certain level of social welfare or security either for the whole population or for certain population groups. Social policy usually affects income distribution and the system of *social security*.

Social security: The institutions and measures of *social insurance* and *social assistance* aimed at providing existential security to the population. There are five 'pillars' of social security, i.e., (1) pensions and survivor benefits, (2) health care, sickness and disability transfers, (3) family benefits, (4) social assistance and (5) unemployment support.

Social insurance: The main component (in most countries) of *social security*. It includes those pillars which depend on previous employment history and, in general, are independent of a claimant's personal or family income (pensions, health care, unemployment support). In some countries family benefits are also considered part of social insurance. Benefits are financed from contributions which may be levied on any combination of workers, employers and the state. Individual benefits are not in most cases related actuarily to contributions.

Social assistance: State-financed means-tested public transfers provided to people in need who meet certain eligibility conditions for regular or occasional income support.

Social minimum: Level of personal or household income which is regarded necessary for a person or a family to exist in a given society without major deprivations.

Social expenditure: Expenditure of the government and public *social insurance* funds on health, education, public housing, child care and public amenities, etc., as well as public cash transfers to families.

Stabilization policy: Macroeconomic measures aimed at 'stabilizing' the external and internal deficits of a country and at controlling inflation in the short term, often by short reductions in the level of economic activity. Relatively little weight is given to maintaining or resolving economic growth, which in stabilization is treated as a longer-term issue.

Subsistence minimum: Minimum income needed to provide a bare subsistence in a given society. It is usually associated with the absolute poverty line and involves major deprivations.

U5MR (Under-5 mortality rate): Annual deaths of children under five years of age per 1,000 live births. More specifically this is the probability of dying between birth and five years of age.

Universal benefits: These benefits are made available to people independent of employment record or income. They may be in cash, such as family allowances, or in kind, as with the provision of 'free' health care.

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G.A.C. and S.S.

Preface

In the mid 1980s UNICEF issued a call for priorities to protect children when making economic policies under the title 'Adjustment with a Human Face'. This set forth an agenda of practical actions to ensure that the health, nutrition and other basic needs of children and other vulnerable groups were protected, and even advanced, while facing the harsh economic realities of coping with recession, restructuring and debt. The ideas, though initially treated with doubts and scepticism, are now accepted as part of basic orthodoxy. Adjustment ought to take account of basic human needs from the beginning, for sound economic reasons, as well as for reasons of human welfare and political acceptability.

In east and central Europe, the need for adjustment with a human face re-appears in a new setting. Here the challenge is to protect children and other vulnerable groups while the economies are going through the throes of 'transition from a socialist to a market-oriented form of economic organisation'. The process will be far from easy. The transition itself seems likely to take longer and be more traumatic than was first envisaged. Moreover, the starting points in terms of the human welfare of the population and infrastructure for basic services now appear much less satisfactory in most countries than was earlier believed. Thirdly, the amount of financial support from outside, and the vitality of the Western economies as markets or as sources of private investment, is well below what was envisaged before.

Thus, the policy choices facing most of the countries of east and central Europe as they go through transition will be tough and painful. The temptation will be to adopt measures which, directly or indirectly, will cut back on the essential needs of children. The risks of this happening will be all the greater if there is no adequate system of monitoring child welfare, so that public and professional attention becomes pre-occupied with inflation, growth and other economic indicators of performance with nothing to attract attention to more direct measures of human welfare such as nutrition and child growth.

This study explores how these dangers can be avoided, by protecting vital human needs in the short-run and by incorporating concern for basic human needs into the economic policies and social welfare infrastructure of the countries in the longer run. UNICEF commends this study to all concerned with children in east and central Europe.

James P. Grant
Executive Director
United Nations Children's Fund (UNICEF)

Introduction

by Giovanni Andrea Cornia and Sándor Sipos

Since the early 1970s, the welfare of children and other vulnerable groups has improved only marginally and, in some cases, even stagnated in all the countries of central and eastern Europe. The most dramatic illustration of this social crisis is the total stagnation between 1970 and 1990 of infant mortality rate in the Soviet Union and the shortening of life expectancy at birth in many countries of the region over the last 20 years. These problems were the result of the failures and biases of public policy in the field of health care and health promotion, housing, nutrition, education and social assistance and of the lack of the most basic environmental protection.

The main cause of the stagnation in living conditions has to be seen, however, in the protracted lack of political freedom and in the poor performance of the economy since the early 1970s. In the relatively simple economies of the 1950s and 1960s, central planning had been able to achieve significant growth and some increases in basic living standards and social conditions. The decline in economic performance started to emerge, however, in the early 1970s, it gradually intensified in the 1980s and reached unmanageable proportions towards the end of this decade. In addition, the pattern of economic development based on heavy industry contributed to severe ecological degradation and the worsening of the health status of the population. Children, for instance, became increasingly affected by respiratory, allergic and degenerative diseases. By the late 1980s, a total and radical overhaul of the political and economic system had become therefore unavoidable.

The transition to democratic pluralism and the market economy can certainly be considered one of the most important events of this century. It has already generated enormous political benefits as well as considerable hopes for economic prosperity and betterliving conditions throughout the region.

All countries of central and eastern Europe have now introduced, and are still introducing, profound changes in economic and social policies.

Macroeconomic stabilisation, microeconomic and sectoral restructuring, and privatisation constitute the main reforms in the economic field, while social policy has so far focused on the creation of safety nets against poverty and unemployment.

Hungary, Poland and Yugoslavia are the front-runners in this process of transformation. For obvious reasons, this process has been even faster in the eastern part of Germany, after reunification. But, also, Bulgaria and Czechoslovakia have already introduced far-reaching changes in early 1991, while some price liberalization and devaluation has already taken place in the Soviet Union.

In contrast, the coverage and focus of safety nets have been limited. In spite of the growing difficulties of the economic reforms and the preliminary evidence of greater social costs than expected, distributive issues and social policy have remained, by and large, a marginal topic in the debate about the transition to the market economy.

While the situation of children was certainly not satisfactory prior to the reform, and while it is not always easy to make clear distinctions between the problems caused by the protracted crisis of socialism and those caused by the economic and social reforms, it appears that the drastic and sudden decline in household income, social transfers, and, in some cases, social expenditure on health, education, and child care makes the transition painful for many children.

In particular, as the economic reforms — which this book considers desirable and necessary — faced problems of implementation, the safety nets for vulnerable groups appeared to be inadequately funded and affected by design problems. In Poland, for instance, safety nets in 1990 were set up on the assumption that household income would decline by less than 5-10 per cent, that inflation would be eliminated within four months, and that unemployment would not exceed 400,000 units by the end of that year. In contrast, by the end of that year, unemployment was three times as great, household income had declined by 27 per cent and unemployment was three times the figure expected.

While the situation has not reached crisis proportions, there are already clear signs of growing poverty among children and other marginal groups, declining food consumption and attendance in kindergarten, reduced availability of certain essential drugs and a gradual but worrying increase in homelessness. While there are strong and genuine hopes that the situation will improve in the long run, it is feared that greater social costs could be incurred over the next few years and that the "worst is yet to come" as suggested by recent developments in the eastern part of Germany.

National governments and the international community are starting

to react to this situation as underlined, for instance, by the rapid increase of World Bank and European Community staff and resources in this field. This book is a contribution to the growing debate on how to minimize the social costs of the transition to the market economy and what social policies could be developed in the years ahead. It argues that, in view of the problems of implementation and sequencing encountered by the economic policies and in view of negative external shocks, broader safety nets and social policies which show more solidarity are required to avoid a further spread of poverty and deprivation among children and other vulnerable groups. Such measures, which are already, if selectively, included in certain countries such as Czechoslovakia and Bulgaria, would require increasing minimum wages, pensions and benefits to adequate levels; more active labour market policies; the preservation of child allowances and their extension to the children of the unemployed or of parents not in the labour force; targeted social-assistance benefits based on objective criteria; full indexation of minimum salaries, pensions and transfers; access to free basic health, education and child care and to specific interventions in school-feeding programmes for children. In addition, to avoid a further spread of homelessness, a gradual liberalisation of the housing market, social-purpose housing and safeguards for the housing rights of large families, low-income pensioners and health- impaired people are necessary. Requisitioning and renovating public buildings and barracks vacated by the army might also be required. And finally, the approach we propose would require setting up a simple 'early warning' child monitoring system, which would also include data on health status and enrolment rates of children, homelessness and a few other indicators. This monitoring system aims at producing a simple 'social monitoring report' to submit periodically to the government and public opinion. In this respect, it reflects concerns similar to those expressed by important international organisations such as the World Bank, the International Labour Office and the World Health Organization, among others. National authorities are also now increasingly concerned. Clearly, their support will remain fundamental if more human focus policies are to be implemented. It is to them that this book is primarily addressed.

This study draws on the UNICEF work on adjustment in developing countries and on its vast experience on child welfare issues. Conditions in eastern Europe are, of course, fundamentally different, but some of the messages are similar. First, there are strong economic arguments in favour of a realistic but extensive social policy characterized by a strong element of solidarity and redistribution. Economic efficiency in most countries of western Europe has been the result, for instance, of massive investment in human capital and of a solid social security system. Second, a sharp

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worsening of inequality and a further spread of poverty among children and other marginal groups could be a major destabilizing factor, prejudicing elements of the economic and political reforms and leading to greater instability. This could likely lead to migrations of biblical proportion to other countries mostly in western Europe. And, third, the call for a more people-sensitive approach to the transition is more than a matter of economic good sense or political expediency. Ultimately it rests on the ethic of human solidarity.

The structure of this book is as follows: Part I presents a series of contributions concerning the region as a whole. Chapter 1 reviews the evidence about children prior to the reform. While much still needs to be done in this field, the greater transparency of facts and figures brought by democratic pluralism allows one to attempt a first inventory on the condition of the child in the 1980s. Chapter 1 deals also with a very preliminary review of available information on changes in child conditions after the reforms were introduced. This part is of necessity of a suggestive rather than a conclusive nature, but the trends it highlights provide useful material for reflection.

Chapter 2 reviews three rather different models of social policy existing in three market economies — the United States, Germany and Sweden — by discussing the efficiency, cost and underlining philosophy of such three different models. One message is quite clear from this chapter, namely, that there is no single 'market-economy' model, and the adoption of one instead of another would lead to very different outcomes.

In chapter 3 a discussion of current trends in social policy prior to and since the economic reform is presented. This chapter highlights also available alternatives. The need for a broader, better financed and more universal approach is identified in this contribution.

Chapter 4 analyzes the components of the economic reforms underway, the problems of implementation they have met so far and the consequences for child and human welfare it has or could produce. This chapter concludes by presenting a number of suggestions for modification of the approach followed currently in several, if not all, countries of the region.

Part II includes four case studies, two from 'early reformers' such as Hungary (Chapter 7) and Poland (Chapter 8) and contrasts them with that of Bulgaria (Chapter 5) and Czechoslovakia (Chapter 6) which introduced these reforms only at the beginning of 1991. These chapters, which have been developed along broadly similar lines, provide useful insights for the countries concerned, as well as empirical evidence and the hypothesis for Part I.

We wish to end this introduction by making it quite clear that our

purpose is constructive. The transformation of the central and eastern European countries is so recent, and the extent of the transformations so enormous, that changes and mid-course corrections will most likely have to be introduced for both economic and social policies. We hope that our efforts may be a modest contribution to the making of future policies that will take the needs of children and other marginal groups into full account.

Part I

Economic Reform, Social Policy and Child Welfare in Central and Eastern Europe

Chapter 1

CURRENT AND STRUCTURAL PROBLEMS AFFECTING CHILDREN IN CENTRAL AND EASTERN EUROPE

Sándor Sipos

Introduction [1]

The opening up of the political and economic systems of the countries of central and eastern Europe has generated considerable hope for political freedom, economic prosperity and better living conditions throughout the region. Ironically, however, this opportunity has also created greater awareness of the problems confronting these nations as open political debate and greater transparency of facts and figures reveal the true conditions in these countries and especially of young people.

While these problems — referred in this study as *structural problems* — are the result of the pattern of social and economic development followed during the last 40 years or so, the abandonment of the socialist model does not automatically imply a solution to outstanding problems. Indeed, solving these problems represents one of the major challenges to the credibility of the newly emerging democracies of Europe. Furthermore, the transition to a market economy and the austerity and reconversion measures, while fully desirable from the perspective of economic efficiency and modernisation, almost unavoidably entail also substantial social costs. Soaring consumer prices due to reduction in subsidies, rising unemployment as a result of industrial restructuring and tight monetary policies have hit the population at large and vulnerable groups in particular. Preventing (to the extent possible) or mitigating these transitional problems is the major challenge for these new democracies.

It is not always easy to make clear distinctions between the problems caused by the protracted crisis of Party-State socialism and those caused by the transition to the market economy — partly because some elements of the crisis are prevalent without fiscal austerity, partly because fiscal austerity is very often the tool of the transition. This functional overlap is further complicated by the fact that the transition started in some

countries (particularly in Hungary, Poland, Yugoslavia) a number of years ago in small, inadequate, incremental steps often without acknowledging the real destination. Also, fiscal austerity was present for a considerable period of time. Many of the problems mentioned hereafter may qualify for both of them. The decision to enlist them among the long-term problems has been motivated by the conviction that the crisis (and the ensuing fiscal austerity) stems back to the original imbalances of the Party-State socialist model.

I. Structural problems of children in central and eastern Europe 1945-1990

1. Child poverty

The *World Development Report* (1990) and also another World Bank study recognized that "deep economic crisis that characterized eastern Europe in the 1980s had a strong impact on average income of the population and on the percentage of people living below the poverty line. The situation deteriorated most sharply in Poland, where the percentage of the poor in total population increased from less than 10 per cent before the crisis to more than 20 per cent by the late 1980s. In Yugoslavia, the increase was somewhat less (from 17 to 25%). In Hungary, the overall poverty rate remained constant" (Milanovic, 1990, 21-2). Poverty statistics are in their infancy in most central and eastern European countries, and there are no standardized child poverty indicators available. Scattered data, however, do provide some evidence about the prevalence and dynamism, and composition of child poverty.

a) In the Soviet Union, the "overwhelming majority of children are in-between official poverty and well being, and about 10-12 million children can almost for sure be considered poor.... In families with low incomes children do not only lack opportunities for adequate recreation and education, they also suffer from lower consumption of most alimentary products" (Riazantsev, 1990, p. 17) (see Table 1.3). In Bulgaria, in 1989, 27 per cent of families lived below the level of social minimum "...and about half of the young families live on the verge of poverty" (Valchev, 1990, p. 14). In Hungary, there was an increase in the number of children living under the poverty line between 1972-87 despite a slight contraction of the overall poverty rate. Their share rose from 32.5 to 40.7 per cent of all poor, whereas the number of all children was the same and the overall poverty rate fell from 15.4 to 13.8 per cent (Andorka, *et al.*, 1990, p. 426; Milanovic, 1990, p. 11; Szalai, 1991. In Czechoslovakia, 4.5 per cent of children are thought to live in absolute poverty in 1990 (see Chapter 6) — up from 1.3 per cent in 1985 (Kovarik, 1989, Table 30).

b) In the 1970s, rural children had a greater risk of falling into poverty than their urban peers. This has changed dramatically during the 1980s. Between 1978 and 1987, the share of urban poor among all poor increased from 48 to 70.7 per cent in Poland and from 24.4 to 47.1 per cent in Yugoslavia (Milanovic, 1990, p. 17). In 1987, in Hungary almost 30 per cent of urban children risked falling into poverty, while for rural children it dropped to 18.2 per cent on the basis of household surveys (Szalai, 1991). In Hungary, the 'traditional' poverty of families with several children has now also reached families with one child only. The ratio of children of small families among the poor has increased from 24 to 25 per cent, whereas the share of these families decreased significantly (from 34 to 17%) among the active population at large. There is a marked shift towards the over-representation of young urban families with children both in the population of the lowest income decile and among those living below the subsistence minimum (Szalai, 1991).

It is very telling that in relatively wealthy and, until now, rather egalitarian Czechoslovakia, 89 per cent of families with one child had a colour television in 1985, whereas 35 per cent of those with two and only 27 per cent of those with three or more children (Kovarik, 1989, Table 25). The clear trade-off between wealth and family size negatively affected the value of the whole family as well (though it was not only a phenomenon restricted to central and eastern Europe).

2. Health problems of children

Infant and child mortality are the most common aggregate indicators of the health status and, more generally, of the well-being of children. All the countries of central and eastern Europe had very high IMR in the

Table 1.1 *IMR in central and eastern Europe, 1950-1989 (per 1000; selected years)*

	1950-55	1960-65	1970-75	1980-85	1985	1986	1987	1988	1989
Bulgaria	92	36	26	18	16	15	15	15	14
Czechoslovakia	54	23	21	16	15	14	13	12	11
Hungary	71	44	34	20	20	18	17	17	16
Poland	95	51	27	20	19	18	18	16	16
Romania	101	60	40	26	25	24	22	22	27
Soviet Union	73	32	26	25	24	23	25	25	25
Yugoslavia	128	80	45	30	23	27	25	25	24
Memo item:									
OECD	42	37	19	11	9	9	9	8	8

Source: Compilation from United Nations (1989, pp. 192-95); World Bank (1990, p. 227); UNDP (1990, p. 147); UNICEF (1991, p. 103).

early 1950s (in the range of 70-130 per thousand). While the improvement in the 1950s and the 1960s was very rapid indeed (see Table 1.1), the 1970s saw a continuing though rather slower improvement in most central and eastern European countries with the notable exception of Czechoslovakia where the gains were marginal and the Soviet Union where IMR has remained in the range of 25-30 per thousand over the period 1965-1989.

Czechoslovakia, Hungary and perhaps Bulgaria further managed to cut IMR by one-third, which was comparable to the rate of progress in OECD countries. In Poland and Yugoslavia the advance was only one-fourth and Romania almost nil. It was only the Czech Lands from the CSFR and Slovenia from Yugoslavia where IMR went down to 10.0 in the whole of central and eastern Europe for the first time in 1989 according to national statistics (Struk, 1990; Todorovic, 1990), but it is still twice as high as today's best Japanese figure (4 per thousand) and still higher than the OECD median (8 per thousand).

Because of this slow decline, the central and eastern European countries lost several places in the overall ranking of countries by level of IMR between 1960-89 (see Table 1.2).

With the exception of Yugoslavia, all central and eastern European countries stagnated or lost rank among the 131 nations both in terms of IMR and U5MR. The most dramatic negative change is recorded in the case of the Soviet Union (sliding down 21-22 places on the IMR list and 22 on U5MR) and, as a surprise, in the case of the otherwise best in absolute value Czechoslovakia (which lost 13-15 places in IMR and 13 places in U5MR). In both countries there was a dramatic increase in the distance from the actually achieved 'best practice' values. The gap widened in the case of the Soviet Union by 387 points in IMR and by 318 points in U5MR and, in the case of Czechoslovakia, by 106 and 56 points respectively. Romania dropped 9-11 places in ranking for both indicators, while, in terms of distance, its deterioration was 244 and 157 respectively. Yugoslavia somewhat improved its position (7-8 ranks in IMR and 5 in U5MR with a 115-point reduction of its distance from the best in U5MR).

The stagnation or slide seen in Bulgaria, Hungary and Poland is not dramatic. However, whereas Bulgaria's distance somewhat increased from the best in IMR, it decreased in U5MR. This seems to be typical for the group as a whole. The relative deterioration of improvements has been considerably greater in IMR than in U5MR, while it appears that among the components of IMR (i.e., perinatal, neonatal and post-neonatal mortality), neonatal mortality is the one which has declined the least (KSH, 1989, pp. 272-99; Valchev, 1990). Despite some improvements in this field in the 1980s, this pattern highlights the problems remaining in the

TABLE 1.2 *IMR and U5MR ranking of central and eastern Europe and other selected countries among 131 nations in 1960 and 1988 and their distance from best levels[1] (best IMR or U5MR = 100)*

Country	Rank		Change	Distance	
	1960	1989		1960	1989
IMR:					
Bulgaria	26	28	−2	306	350
Czechoslovakia	11	24-26	−13−15	169	275
Hungary	27-28	30-31	−3	319	400
Poland	32-33	30-31	+2	387	400
Romania	36-37	45-48	−9−11	431	675
Soviet Union	21-22	42-44	−21−22	238	625
Yugoslavia	48	40-41	+7+9	575	600
Austria	20	8-16	+4+12	231	200
Chile	54	35	+19	713	500
Cuba	32	24-26	+6+8	387	275
Finland	5-7	2-3	+2+5	138	150
Greece	29	24-26	+3+5	331	275
Hong Kong	23-24	4-7	+16+20	275	175
Japan	14-16	1	+14+16	194	100
Portugal	41-42	27	+14+15	506	275
Spain	25	17-18	+7+8	294	225
United States	10	19-23	−9−13	163	250
U5MR:					
Bulgaria	30	29	+1	345	283
Czechoslovakia	12	25	−13	165	216
Hungary	25	28	−3	285	283
Poland	31	31	0	350	300
Romania	33	44	−11	410	567
Soviet Union	23	45	−22	265	583
Yugoslavia	41	36	+5	565	450
Austria	19	16	+3	215	167
Chile	50	37	+13	715	450
Cuba	34	26	+8	435	267
Finland	9	3	+6	140	117
Greece	28	23	+5	320	200
Hong Kong	27	5	+22	320	133
Japan	16	1	+15	195	100
Portugal	40	27	+13	560	267
Spain	24	12	+12	285	167
United States	10	20	−10	145	200

Source: Calculated from data given by *The State of the World's Children 1991*, New York: UNICEF (1991, p. 103).

field of neonatal care [3], of pregnancy and management which are responsible also for the high incidence of low birth weight and high maternal mortality [3]. The variations and inadequate developments in IMR, U5MR and other major child health indicators may be explained by the following factors:

i) A plausible explanation for the comparatively high levels of low birth weight, as well as neonatal and maternal mortality in the central and eastern European countries, is the prevalence of young marriages and of births to teenage mothers. All seven countries are among the top ten in Europe both in terms of the proportion of marriages between 15 and 19 and in terms of teenage birthrates. In Bulgaria, for example, the teenage birthrate is 81.1 per 1000, whereas it is only 6.2 per 1000 in Switzerland. Also, in Bulgaria almost every fifth child is born to a teenage mother. In the other central and eastern European countries, between 8-16 per cent of children are born to teenage mothers. In Switzerland, that figure drops to 1.8 per cent (Wynnyczuk, 1990). Social policy might have unintentionally caused such a situation. In the Czech Lands of Bohemia and Moravia, for example, in 1984, 48 per cent of children were born within eight months after marriage, indicating that "pregnancy represents the main reason for marriage and, at the same time, the first child is the qualification to obtain certain social benefits" or to join the housing list (Struk, 1990). In the Soviet Union, it was observed that the share of early marriages increased mainly in the regions of low fertility rate which partially offset the favourable decrease in the share of children among dependents (in the European USSR it is 55% and decreasing, whereas in the Asian part it is 80-85% and still growing) (Braithwaite, 1989, p. 86; Riazantsev, 1990).

ii) Another problem affecting most central and eastern European countries is the disproportionately high level of IMR differentials by location, ethnic group and social class. While in OECD countries such differentials by region are in the order of 1:1.5, in the central and eastern European countries differentials of 1:5 are not uncommon. Regional and ethnic differences in IMR may not come as a surprise in the Soviet Union which stretches over continents, cultures and levels of economic development. In 1988, the best IMR was 11 per 1000 in Baltic Latvia and the worst, 53.3, in central Asian Turkmenia (Mezentseva, 1990, pp. 873-4; Anderson, 1989, pp. 472-6, 482-6; Goskomstat, 1990a, pp. 175-6) where pockets of IMR above 100 still exist [4]. In Yugoslavia, the situation is rather similar, although the extremes occur in a geographically compressed area. In 1989, the IMR in Slovenia was 10.0, whereas in Kosovo it was 52.1; Kosovo, with less than 10 per cent of the population of Yugoslavia, accounts for almost one-third of total infant deaths in the country (Todorovic, 1990; Mastilica, 1990, pp. 405-7). The same inter-

regional variations can be observed in terms of causes of infant death in these two countries. While only 6.7 infants per 10,000 died of infectious diseases in Estonia in 1986, 174 were victims of the same cause in Tadjikistan. In the same year, in Lithuania, only 10.1 children died due to respiratory problems, whereas 308.7 in Turkmenistan, in Soviet Central Asia (Mezentseva, 1990, p. 874). The same indicators show no less variation in Yugoslavia — infectious diseases: Slovenia 3, Kosovo 124; respiratory problems: Slovenia 2.8, Kosovo 175 (Mastilica, 1990, p. 407).

Regional variations in IMR are also high in other central and eastern European countries somewhat more homogeneous than the Soviet Union and Yugoslavia. In 1988, in Czechoslovakia for example, the best IMR was 9.3 in east Bohemia and the worst, 15.3, in east Slovakia in 1988 (Struk, 1990). In Hungary, where the longest possible distance in the country is hardly more than 500 km, the best figures in the west reached 9.4, while the worst figures in the north-east were still above 20 (KSH, 1989, p. 286; Orosz, 1990, p. 850). In Poland, the difference is also close to 1:2. Rural Walbrzych district shows figures of 12.8, while in industrial Lódz district these rise to 21.6 (ZG TPD, 1990; Duch, 1990, pp. 345-6; Wnuk-Lipinski, 1990, pp. 862-6). In Bulgaria, on the other hand, inter-regional variations in IMR rapidly leveled off from 1:3 in the 1970s to 1:2 in the early 1980s and to 1:1.3 in 1987 (Minev, 1990, p. 844).

iii) Rural-urban differentials in IMR, by contrast, are less marked than those by regions and somewhat more similar to the situation in the OECD countries. Of particular relevance is the situation of Prague, Budapest and some other highly urbanized areas of central and eastern Europe, such as the vojvodships of Lódz and Katowice in Poland, where the negative impacts of urban congestion, environmental pollution and new poverty offset the easier access to medical services and higher average income levels and therefore IMR is higher or equal to that of rural or other less urbanized settlements elsewhere in the country. The Soviet Union and Bulgaria follow the traditional pattern of rural-urban bias inasmuch as rural IMR is substantially higher than the urban one. In the Soviet Union, the figures varied by as much as almost 50 per cent in 1988 (Goskomstat, 1989a; Mezentseva, 1990, p. 873), and in Bulgaria by 32-40 per cent during the 1980s (Minev, 1990, p. 839; Valchev, 1990). In Hungary and Poland, the rural-urban differences in IMR are not significant anymore. In Hungary's capital, Budapest, IMR was hardly better (14.7) than the national average and was way behind most western counties of the country (KSH, 1989, p. 287). In Poland, Lódz, the most urbanized vojvodship in the country (91.5% of the population lives in towns) has the highest IMR (Wnuk-Lipinski, 1990, p. 864-5). In Katowice, every fourth pregnant woman suffers from a pathological condition (Duch, 1990, p. 347). In Czechoslovakia, this trend is even

more developed and the relative position of the capital Prague has been continuously deteriorating. In fact, Prague's IMR (13.7) is 30 per cent higher than the federal average, whereas in east Bohemia and south Moravia, regions with stable settlements and significant agriculture, IMR has been lower for decades than in the traditionally industrial regions of north and west Bohemia (Struk, 1990).

iv) Despite the greater equality in income distribution (see Atkinson, 1991), IMR differentials by social class and education levels appear to be quite pronounced and at least as great (or greater) than in OECD countries. In addition, the single most important risk factor was found to be the level of education of the parents. In Poland, for example, children born to mothers who did not complete elementary school face a risk of early death which is three times as great as those born to mothers with a university degree (Wnuk-Lipinsky, 1990, p. 862). This ratio is somewhat higher in Hungary (Orosz, 1990, p. 851) and almost 1:5 in Yugoslavia (Mastilica, 1990, p. 409). Similar differences appeared between families with their first child and families with more than four children (13.8 and 26.3 in Poland; 12.8 and 34.9 in Hungary respectively). In Hungary, IMR rates were also more than double between children born in families where the breadwinner was university-educated (10.4) and children born to peasants in state agriculture (21.3) (KSH, 1989, pp. 118, 276, 278-9). This statistical profile suggests that a slow-down in social mobility, marginalisation and pauperization may reverse the gains in IMR obtained by the more achieving sectors of society.

v) In spite of scarce empirical information, IMR differentials appear to be substantially greater for a number of ethnic groups. In Yugoslavia and the Soviet Union, ethnic differentials in IMR correlate closely with regional differentials. In other countries where such correlation is weaker, because of the different pattern of distribution of the population by region, scattered data on IMR by ethnic groups point to much higher IMR rates for the Gypsy population. A unique survey carried out by the Ministry of Health in the Czech Republic shows that IMR among the Gypsy population is 2 to 2.5 times higher than that of the non-Gypsy population. The incidence of low birth-weight deliveries is 2-5 times higher in Gypsy communities in different parts of the Czech Lands than the national average (Struk, 1990). The same phenomenon was recorded in Hungary where the incidence of low birth weight was 9 per cent for non-Gypsy, and 20.2 per cent for Gypsy deliveries in a large sample between 1981-84 (Kóbor, 1988, pp. 251-5). In Bulgaria there are indications that infant morbidity, and especially for certain specific causes (e.g., hypotrophic infants, rickets), is higher in areas where there are considerable clusters of ethnic Turks (Minev, 1990, p. 844).

vi) While infectious diseases among children in central and eastern

Europe have decreased (with the exception of the USSR), there has been a marked increase in the number of environmentally induced diseases, especially respiratory diseases, cancers and congenital malformations. In addition, injuries related to accidents have increased as well.

In central and eastern Europe, Czechoslovakia, Poland and certain parts of the Soviet Union are the most exposed to environmental pollution and its implications. One-fifth of the 15 largest sources of toxic emissions in Europe are situated in the Czech Republic, according to the monitored principal indicators of environmental pollution (SO2, NOx, dust). Czechoslovakia is the most polluted country in the world in terms of toxic emission per capita. In Poland, 27 administrative units with around one-third of the population are classified as seriously affected by environmental pollution, most badly the Katowice district in Silesia[7], according to the Polish Ministry of Health and Social Welfare (Duch, 1990, pp. 345-6; Norska-Borówka, 1990, pp. 1392-3). It is difficult to discuss similar situations in Romania and in the Soviet Union as information on environmental issues was politically discouraged until recently. However, the disasters at Chernobyl or Lake Aral have captured the attention of the world. It is now recognized that major environmental catastrophes have happened in the Soviet Union and that there is a considerable potential for more[8]. Some 17 per cent of the territory of the Soviet Union, which is home to 26 per cent of the population, has been declared an ecological crisis area. Almost 25 per cent of children in these disaster areas are born with genetic abnormalities, according to the estimates of independent Soviet environmental movements (Shcherbak, 1991). Bulgaria, Hungary and Yugoslavia are also exposed to considerable problems due to pollution.

A massive increase is reported in the incidence of extrinsic respiratory diseases all around central and eastern Europe, although infant mortality due to respiratory diseases declined in most countries due to improved treatment. In Czechoslovakia, pre-school-age children are the most affected and are treated for respiratory problems, on average, five times a year (Struk, 1990). In Hungary, the number of extrinsic respiratory diseases doubled between 1985-89 (Ranschburg, 1990). In particular, bronchitis grew 2.5 times and asthmatic diseases five times during the last decade (Orosz, 1990, p. 852), while it increased by 20 per cent in Yugoslavia between 1979 and 1988 (Todorovic, 1990). In Poland, there has been a 70 per cent increase in children's bronchitis over the last decade in the Cracow area where at least 10 per cent of children suffer from chronic respiratory diseases (Bialic, 1991).

The number of allergy cases among children has been increasing by 10 per cent, on average, during the last decade in Czechoslovakia, while, in especially exposed areas, the increase exceeded one-third (Struk, 1990).

Similar developments have been recorded in Poland (Duch, 1990, p. 346).

The incidence of tumor diseases among children more than doubled between 1975 and 1988 in Czechoslovakia (see Chapter 6, Table 6.7), but due to improved medical treatment, mortality caused by malignant tumors has declined (Struk, 1990). The same applies to Silesia in Poland (ZG TPD, 1990). In the Soviet Union, in the zone contaminated by the Chernobyl disaster, the thyroid glands of 43 per cent of children underwent a swelling and a five-fold increase in thyroid-gland cancer incidence is forecasted. Leukemia has increased 2-3 times since the disaster (Shcherbak, 1991).

Nitric and arsenic pollution of drinking water reservoirs is an acute and increasing problem in Hungary where the number of settlements without healthy drinking water increased from 300-400 in 1970 to 700 in 1988 and where almost 1,500 infants were treated for problems caused by the high nitrate content of the water between 1975-85 (Orosz, 1990, p. 852). Similar deterioration is observed in Poland where half of the public wells have been banned by the sanitary authorities (Duch, 1990, p. 346).

In Poland, Czechoslovakia and the Soviet Union, there are large areas where these environmental hazards overlap and the negative health implications are concentrated. In the highly polluted Katowice district, unlike other parts of Poland, IMR is increasing [9], the share of high-risk pregnancies is 45 per cent, while the incidence of premature deliveries is an unusually high 14-20 per cent (Duch, 1990, p. 346; Norska-Borówka, 1990, p. 1393). In the Cracow area, another heavily polluted part of Poland, a study has shown that one-third of all women tested after delivery had spontaneous abortions in the past, whereas in a control group in a less polluted area this ratio was less than 10 per cent (Bialic, 1991).

vii) Universal access to health care institutions was in principle provided free or with limited charges for all children in central and eastern Europe (access was somewhat restricted by the uneven geographical distribution of the facilities). However, private peasantry and non-organized artisans did not always have free access to health care, while in some countries certain strata of the society was *de facto* left out of the national health system. In Romania, for example, because of strict residency rules, many people settled illegally in large towns where they could not register for any territorial social or health assistance records (Radulian, 1990). Similar complications with residency registration occurred in other countries as well. In Yugoslavia, there are some 2 million children who are not covered by the national health-care system. Of these, the largest group is the 1 million children whose parents work abroad (Todorovic, 1990).

The health system was under considerable strain in most countries because it was not adequately funded (usually allocations to it were

around 4-8% of GNP) and it had to perform multiple functions such as making up for non-existent (and ideologically denied!) social services (Struk, 1990). In many countries, children or very old people were kept in hospitals because they needed permanent assistance, but there were no social institutions which could provide it for them outside the health care system. Obviously this burden contributed to the low efficiency of the system.

viii) Female employment in some countries of central and eastern Europe runs to very high levels and this can be the source of difficulties. In Czechoslovakia and Hungary, 75 per cent of working-age women are in the labour force. In Romania, women constitute 45 per cent of the total labour force which involves very high female participation (in agriculture their share is 57.3%). In Poland, 70-75 per cent of women are employed. With virtually full employment, it is clear that even if the whole child and family support services were to exist and function smoothly (which they do not), there remains the problem of almost full daytime institutionalization of child care. This can prove to be inadequate if, for example, a child is sick for a long period of time (even grandparents have been largely restricted in their support because they also work). Provisions for paid or unpaid leave for care in case of sickness have been provided but on a limited scale. Full employment for women presupposed universal preschool participation from the age of three and three years maternity leave and allowance. But this was not really provided in these countries (with the notable exception of Hungary and Czechoslovakia). Another alternative is an expanded crèche system for the day care of children 0-3 years old. However, this was provided for only 20 per cent of children even in Hungary and Czechoslovakia. It is now generally acknowledged that institutionalization of very young babies should only be the last resort.

In the Soviet Union, some 50 per cent of women of working age have been employed over the last 20 years. This is not a very high figure compared with other countries in central and eastern Europe. In the Soviet Union, however, the prevalence of women in harmful and heavy manual jobs is very high (Goskomstat, 1989b, pp. 39-43). According to a recent study, it has been shown that, of the total number of workers occupied in heavy manual labour in industry, one-fifth are women. In construction they number more than one-fourth. Among workers working under severe and harmful conditions in industry, 44 per cent are women. In construction and road building, this ratio is 17 per cent and rises to 34 per cent in railroad repairs. Some 2.7 million women are employed in jobs which fail to meet labour protection norms, while 38 per cent of those who work the night shift in the Soviet Union are women. In industry in general the majority of women are helpers: loaders, transport workers, etc. (Labetsky, 1990, p. 33). This can be very dangerous espe-

cially during pregnancy because excessive physical effort or exposure to harmful substances can often result in spontaneous abortions, premature and low-weight babies.

3. Nutritional problems

A thorough study of central and eastern European food consumption levels and an international comparison would not show a particularly alarming picture. The three major problems are: an unbalanced diet and micronutrient deficiencies, insufficient nutrition among low-income groups, and a low rate of breastfeeding.

a) The high consumption of animal fats, sugar, salt, bread and alcohol together with a low intake of good quality meat, fish, and other sources of protein, vegetables, fruit and vegetable oils are a characteristic of diet in central and eastern Europe countries. Although there are regional variations, the overall effect is negative with regard to the diet of children. Later on this can be very easily related to high incidences of cardiovascular problems and shorter life expectancy than in western European countries. Throughout the decades of the 'socialist experiment', nutrition policy was not based on scientific principles of healthy nutrition but on short-term economic advantages which curbed economic decline (Struk, 1990, p. 10).

In Poland, barely 50 per cent of the children drink milk regularly and about 10 per cent do not drink milk or eat cheese or other dairy products. An estimated 10-20 per cent of school children go to school without breakfast, and about 30-40 per cent of all children have no school meals at all. Thus, around one-third of pupils go hungry in school. Although protein and vitamin deficiencies are not yet critical, even smaller further deteriorations could worsen the situation disproportionately. Rural children are in a particularly difficult situation (ZG TPD, 1990). Surveys in Czechoslovakia and Yugoslavia show that food in pre-school institutions was nutritionally 'bad or inadequate' (Struk, 1990; Todorovic, 1990).

b) It is more alarming that there is a huge variation in food consumption patterns according to income levels. In the Soviet Union, (see Table 1.3), families with a low income consume hardly more than one-third of meat and fish and half of milk or fruit of those with a high income. Even their potatoes and sugar consumption seems to be limited by their low income.

Low income families in the Soviet Union consume more bread than their wealthier counterparts and their diet is kept in balance by a high consumption of milk and dairy products. This positive anomaly is most likely to be explained by heavy subsidies on milk and dairy products [10], despite the scarcity and inferior quality of this latter group. In 1985, 13

TABLE 1.3 *Consumption of food by families with different aggregate per capita income in 1986 in the Soviet Union (kg/capita/year)*

	Aggregate monthly per capita income, Rbl			
	-75	75-100	100-150	150-
Meat and products	32	51	66	86
Milk and dairy	224	314	363	448
Eggs (individual)	139	211	247	302
Fish and seafood	7	12	15	19
Sugar	23	28	31	37
Oil and fats	9	8	7	8
Potatoes	71	95	102	119
Vegetables & melons	80	89	96	115
Bread and farinaceous	146	125	112	120
Fruit	34	41	48	61

Source: Family budget survey data (Goskomstat, 1988; Riazantsev, 1990).

million families, and, in 1988, 7 million families had less than 75 roubles/capita/month income, or 17.9 and 9.6 per cent respectively (Braithwaite, 1989, p. 58). Some 60 per cent of these families were young and large. Even in 1989, around one-third of all children (27 million) suffered the nutritional bias reflected by Table 1.3 living in families with less than 100 roubles/capita/month income out of which 10-12 million lived in families under the 75-78 rouble poverty line (Riazantsev, 1990).

The same anomaly with subsidized milk can be observed in all central and eastern European countries, with the exception of Yugoslavia where it is not so obvious [11]. In Hungary, annual per capita milk and dairy consumption declined by 18 per cent (from 194 to 160 litres) between 1988-90 as prices started to rise [12] (see Chapter 7). This indicates that if subsidies on milk and dairy products (common in all central and eastern European countries during the last 40 years) are reduced or eliminated without adequate compensation, milk consumption will fall drastically and hit children all the more, as milk as a source of protein is exceptionally important for their development.

c) Problems related to breastfeeding are universal and are very much manifest in central and eastern Europe. Breastfeeding rates are very low in comparison with an overall figure of 67-95 per cent for the majority of European countries. In Poland, in 1988, only 25 per cent of children were breastfed at the end of the third month and 13 per cent in the sixth month (ZG TPD, 1990). In Bulgaria, the overall rate of breastfeeding is 63 per cent (Valchev, 1990). In Czechoslovakia, between 1983-1987, the rate of children being breastfed until the end of the third month varied between 28 per cent to almost 35 per cent, and between 7.2 and 10.9 per cent until end of the sixth month. More than 6 per cent of children are

not breastfed at all (Struk, 1990). More educated mothers living in urban centers generally breastfeed for longer periods than the less educated or rural mothers. Inadequacy of breastfeeding becomes a critical question when milk substitutes, formula milks and quality baby foods are in short supply, which is the case in most of these countries (see Part III).

4. The housing problem

The housing situation is unquestionably more severe than the nutritional one and it hits young couples with children in particular because they face greater overcrowding and because children are more vulnerable to its negative impacts (e.g., hygiene, psychological and cognitive development). The two most important factors causing hardship to families are: difficult access to housing due to short supply, inadequate size and poor quality of the housing itself.

a) Construction has always been unable to keep up with the pace of demand which was fueled not so much by population growth, but by changing family patterns (nuclear family pattern) and massive relocation of the population. In the Soviet Union, housing problems are exceptionally acute and severe. Even very large families have to wait for a very long time for better housing (see Table 1.4), and in almost 17 per cent of families with four children this meant more than 10 years. Almost 52 per cent of families with three children have been on the waiting list for more than five years.

Table 1.4 *Distribution of large families according to waiting time for better housing in the Soviet Union in 1989 (%)*

No. of children under 16	Years of waiting					
	0-1	1-3	3-5	5-10	10 >	Total
3 children	3.4	23.3	21.5	36.7	14.8	100
4 children	3.9	24.1	24.3	31.1	16.6	100
5 and more	4.7	29.0	25.3	30.6	10.4	100

Source: A sample survey of 310,000 families, March 1989 (Goskomstat, 1990c).

The housing policy of the Soviet Union, unlike some other central and eastern European countries, had not encouraged private construction for a very long time and therefore people could not improve their housing situation by private efforts. This definitely contributed to an increasing desperation in many families and eventually to divorce, alcoholism and delinquency.

In Yugoslavia, on the other hand, private construction has long been promoted and the overall number of housing units is largely equal to the number of households. However, there is a real shortage of flats (640,000 units, or 10.5% of total housing stock). Of these, 470,000 are in towns. Less educated workers are less likely to have access to public housing than white-collar workers, and therefore they try to solve their problems on their own. Apart from the usual problems of private construction in central and eastern Europe, in Yugoslavia there is an added dimension of failure to integrate these private efforts into urban development plans and mainstream standard regulations which has resulted in a large number of unregistered constructions which lack the supporting utilities. This is especially common among the Gypsy population who have set up shanties outside major towns. In certain parts of Yugoslavia, one can speak of urban *shanty* sprawl which is socially very dangerous. There are studies which already show the high prevalence of juvenile delinquency, malnourishment and other forms of physical or mental retardation among children from these slums (Todorovic, 1990).

In Bulgaria, Czechoslovakia, Hungary, Poland and Yugoslavia, there is an increasing differentiation between the private and the continuously shrinking state sectors of construction activities in terms of speed, cost and quality. The steady deterioration of state-owned and administered housing stock became a subject of ridicule throughout central and eastern Europe long before the political transition started.

b) Despite all private efforts (where these were allowed and encouraged), the housing situation in most countries has remained a major source of frustration for a large part of the population. In Bulgaria, where flats are small (average 68 m^2) but where 85 per cent of housing is privately owned, 16 per cent of families with children (802,000 children under 14) live in shared or sub-let premises. About 1.5 million families, with half of the child population, have no separate room for the children and 6 per cent of the population live in dwellings with less than 6 m^2 per capita and 43.1 per cent with less than 12 m^2 (Valchev, 1990). In Czechoslovakia, access to living space sharply deteriorates with the number of children (see Table 1.5).

Children living in families with more than three children have an extremely reduced living space compared to the average. Gypsy families are generally in a specially disadvantaged situation which partially reflects their bigger family size and limited access to housing. In Hungary, a sample survey has shown that the likelihood of delivering low-weight, premature babies increases in relation to the number of persons living in the same room with the pregnant woman (Ranschburg, 1990). In Romania, there was a particularly rapid relocation of population from agriculture to industry and from rural to urban settlements. New urban

TABLE 1.5 *Living space per person and index of crowdedness in apartments according to the number of children and in Gypsy households in Czechoslovakia, 1987*

Type of household	Index of living space per person	Index of crowdedness
Average	100	100
Complete households		
with 1 child	91	106
with 2 children	82	117
with 3 children	71	137
with more than 3 children	53	189
without children	117	87
Gypsy households	49	208

Source: Struk (1990, p. 18).

apartments were often built in a makeshift manner which resulted in very low-quality housing stock (often with no bathroom and with the toilet along the corridor). Housing policy sometimes followed explicitly totalitarian guidelines (forced centralisation of the population in well-controlled urban blocks of flats instead of in scattered rural settlements with a higher level of personal autonomy) and construction regulations were time after time subject to peculiar regulations in order to save on lighting and heating costs (Radulian, 1990). Some 15 per cent of the population of the Soviet Union live in 'communal apartments' which actually means sharing living space with other people or families. About 10 per cent of young families rent only a room or part of a flat. The maximum floor space per person to qualify for the waiting list is 6.3 m^2, or even less in some republics, and the average size of flats is 58 m^2 (Riazantsev, 1990).

5. INADEQUATE CHILD-PARENT INTERACTION - 'SOCIAL ORPHANS'

Inadequate child-parent interactions can cause serious drawbacks in the psychological and cognitive development of children. In many cases, the lack of communication is a prelude to neglect, abandonment or delinquency. Two aspects of this problem are discussed here: the implications of the socialist modernisation experience for family cohesion and the role of support services and institutions in facilitating the efforts of families to adjust to modernisation:

a) Modernisation has generally entailed a certain degree of family break-up and instability. The Soviet Union is the first in Europe in terms of divorce (3.4 per thousand), while Hungary (2.8) and Czechoslovakia (2.5) are not far behind (Wynnyczuk, 1990). In addition, family values have been undergoing tremendous changes, even in those countries where divorces were not so prevalent [13]. Modernisation and massive relocation

of people without adequate living conditions greatly contributed to the loosening of family ties in central and eastern Europe. In Hungary, Poland and Yugoslavia, expanding second economy activities, overtime work, moonlighting or working abroad were seen as the only way, by most families, to achieve decent housing conditions — a separate room for the child (Gábor, 1979). Thus, a considerable part of the negative social consequences of overwork on families and the life of children can be traced back to the inadequate housing supply. In countries where official distribution was virtually the only way to acquire a flat, children were often conceived as a means of entitlement rather than wanted in their own right (Struk, 1990).

'Latch-key' children are common everywhere in the area and communication with parents is generally insufficient. This may easily lead to the creation of 'social orphans' and to the weakening of solidarity between generations. According to broad criteria [14], almost one-third of Bulgarian children may fit into this category (Valchev, 1990). In Czechoslovakia, this figure seems to be much lower but has definitely been increasing during the last 40 years (Struk, 1990). In Hungary, the number of children 'at risk' (with alcoholic or criminal parents, or who are on the verge of delinquency or maladjustment) was estimated at 500,000 in 1990, or 17 per cent of the child population (GYMF, 1990, p. 71). In Romania, prohibition of contraceptives and abortion substantially contributed to the rise in the number of unwanted children. Not all of these children became legally abandoned, but many of them are largely neglected by their parents (Radulian, 1990). In Yugoslavia, the number of children monitored by social institutions increased by three times between 1974 and 1989 (from 60,000 to 183,000), with children of divorced parents constituting the largest and most rapidly growing sector (Todorovic, 1990).

b) Pre-school education and child care are important because a large proportion of mothers work and pre-school education has, in fact, become part of the formal education process. The absence of these services is therefore a source of frustration for working parents, yet over-reliance on them reduces child-parent interaction. There were always two principles in the provision of these services in central and eastern Europe. One was that the state should provide for all and, second, that large companies or institutions should have their own facilities. There are certain variations in the provision of these services in central and eastern Europe, although coverage is usually high (see Table 1.6). With the exception of Czechoslovakia, the kindergarten system does not cover the whole child population (although Bulgaria and Hungary come close to it). Rural areas lack pre-school institutions in Poland and the Soviet Union. In Yugoslavia, there are hardly any kindergartens in villages and even in towns they are

attended mainly by children from middle-class families. So instead of equalizing social chances, the kindergarten system has tended to increase differences (Todorovic, 1990). Altogether, however, the kindergarten system in central and eastern Europe does not fare badly in international comparison. The attendance rate is high and the provisions are good and relatively cheap.

TABLE 1.6 *The ratio of 3- to 6-year-old children attending pre-school institutions in 1986-89 (in percentage of the age group)*

Country	Ratio		
	Urban	Rural	Total
Bulgaria			82
Czechoslovakia			96
Hungary			86
Poland	58	38	50
Romania			78
Soviet Union	69	40	58
Yugoslavia			20

Source: Goskomstat (1990a, p. 82); Kovarik (1989, Table 38); HCSO (1990, p. 67); Radulian (1990); Todorovic (1990); Valchev (1990); ZG TPD (1990).

Access to crèches (0-3 years) is limited everywhere. In Hungary and in Czechoslovakia, attendance is around 20 per cent, elsewhere less. This has, however, to be seen in the context of long maternity leaves which often stretch over two or three years.

In elementary schools, supervision after class is provided for pupils whose parents work, although the coverage is usually limited (39% in Hungary, none in Bulgaria). Due to the deterioration in real income and increased fees, growing numbers of poor parents are not able to pay either the daytime supervision or the meal for their children. The central government stopped subsidizing supervision in 1991 and local governments are unable to finance it. Thus, many unattended children may end up as 'latch-key' kids (Ranschburg, 1990).

6. DEVIANCE AND DELINQUENCY AMONG CHILDREN AND ADOLESCENTS

In the most idealistic days of socialism, crime and delinquency were regarded as remnants of capitalism and were supposed to vanish with the rise of true socialism. Drug abuse was a taboo until even recently. Little research and attention were focused on these issues. The negative consequences of this willful and protracted neglect have not prepared society

for effective remedial action once it was no longer possible to ignore the phenomenon anymore.

a) The available figures suggest that in most countries in western Europe and the United States, juvenile crime [15] rapidly increased during the 1960s and 1970s, after which it stabilized and in some cases somewhat declined during the 1980s. In central and eastern Europe, there has been a steady growth in the number of juvenile crimes. In Czechoslovakia, theft (including crime against state property), bodily harm, prostitution, sexual aggression and rowdyism are the most common forms of juvenile délinquency. Delinquency increased in the 1980s from 109 per 10,000 in 1980, to 143 in 1987. The proportion of Gypsy delinquents is high (around 23% during the period 1980-87). But this may be the result of reporting bias. In 1980, the delinquency rate among Gypsy youth aged between 10-18 years old was 560 (per 10,000 Gypsy youth) (Kovarik, 1988, Tables 47, 64, 68). In Hungary, the number of criminal cases involving adolescents grew almost constantly between 1963 and 1988 from 2,500 to 6,741, which corresponds to 83 and 218 cases per 10,000 respectively — a large increase indeed (KSH, 1989, p. 292; GYMF, 1990, Table 45). In Bulgaria the number of juvenile offenders brought to court is not too high (55-60 per 10,000), but the prevalence of juvenile delinquency is alarmingly high among Gypsy children (Valchev, 1990). There is little factual information available about Romania where there was little common ground between social reality and official rhetoric. This has allegedly contributed to the increase of delinquent behaviour because "a double-dealing attitude was a chance to survive" and it thus became an acceptable norm (Radulian, 1990, pp. 6-7). The same gap between official education and real life was observed in the Soviet Union where more than 1 per cent of the child population was arrested in 1989 for delinquent behaviour (Riazantsev, 1990). The number of juvenile crime cases grew by 11 and 14.9 per cent in 1988 and 1989 respectively. The increase was particularly sharp (55%) in the large urban centres such as Moscow and Leningrad, which could be accounted for 80 per cent of the overall increase in juvenile delinquency in 1989. One-third of all crimes in 1989 were committed by children under 18 years of age. Apart from the social and family problems mentioned elsewhere in central and eastern Europe, in the Soviet Union, the lack of facilities and possibilities for entertainment also contributed to delinquency (Labetsky, 1990). In Yugoslavia, the number of children with registered behavioural problems has broadly stagnated. However, the crime rate has fallen over the last 10 years by almost 20 per cent. This may be explained by social work and an increase of some 200 per cent in institutional care and other social services (Todorovic, 1990).

b) Central and eastern Europe is still believed to be less exposed to

drug abuse than western Europe or the United States [16]. There is, however, an increase in children affected by drug abuse in Bulgaria, and this even includes youngsters under 10 years old (Valchev, 1990). According to a large survey in 32 schools in the Czech Republic, abuse of sedatives was admitted by 10 per cent of the respondents and experiments with various drugs by 3 per cent (Struk, 1990). In Poland, according to anonymous questionnaires, 3-5 per cent of primary school pupils in big cities are affected by some form of drug abuse and about 30-40,000 children of primary and secondary school age are thought to have become addicts (ZG TPD, 1990). In 1989, only 6,700 young drug addicts were registered by the authorities, but conservative estimates put the realistic number at least five times higher (Labetsky, 1990).

c) According to the same survey, in Czechoslovakia, 25 per cent of pupils under 15 have already been drunk. In Poland, the situation is similar. In the same age group, 16.5 per cent of the boys and 4.5 per cent of the girls drank alcohol to the point of intoxication; 10 per cent of children are considered seriously endangered. The number of children exposed to the danger of becoming alcoholic in Hungary increased by 2.5 times between 1971-87, from less than 0.4 to 0.9 per cent of the total child population under 18 (Ranschburg, 1990). 1.3 per cent of 14-19-year-olds consume alcohol regularly (GYMF, 1990, p. 55). In the Soviet Union, alcoholism is a real danger for 13 per cent of the school-age population who consume spirits regularly (Labetsky, 1990).

7. Institutionalization of children

International attention has focused on the status of institutionalized children in central and eastern Europe (Himes, 1991). In general, excessive centralization of power in the hands of the Party-State and ideologically motivated ignorance can be blamed for the high rate of institutionalization and the dismal 'institutional culture' in much of central and eastern Europe. Three aspects of this problem include: the number of children in institutions, relations between institutions and society, and relations within the institutions.

The degree of institutionalisation of children can be seen as high in some central and eastern European countries. In western European countries, the number of children in institutional care is normally under 1 per cent. In some central and eastern European countries, this indicator is much higher [17]. Romania tops the list with a figure between 2.4 and 3.4 per cent (the higher figure if those in preventive justice are also included). This can be partly explained by the long-prevailing rigid anti-abortion policy (Kessler, 1990, pp. 1, 7-8). But this may now be changing with new legislation (Pierotti, 1990). Bulgaria and Hungary have an

institutionalisation rate of around 1.4 per cent of children (Valchev, 1990; KSH, 1989, p. 240; GYMF, 1990, p. 23), and Czechoslovakia and the Soviet Union around 1 per cent (Struk, 1990; Kroupová, 1989, p. 45) or 0.7 per cent in the case of the Soviet Union if those in criminal institutions or preventive care are excluded (Goskomstat, 1990a, p. 84). Only in Poland (0.5%) (ZG TPD, 1990) and in Yugoslavia does the figure fall well bellow 1 per cent (Todorovic, 1990).

It is difficult to prove or quantify the damage done by closed institutions, cut off from the rest of society, where conduct and even policy often ignored the interests of those in their care. Rehabilitation of the disabled, handicapped, abandoned and socially deprived enjoyed lip-service in all central and eastern European countries. But institutionalization as the overriding solution has prevailed. As far as the conditions in these institutions are concerned, the following list of problems from Hungary may serve as a summary for all:

— The condition of the buildings and the quality of equipment are at a very low level.

— Professional qualifications are rather low and staff often have the wrong personality to deal with children.

— In most institutions, very aggressive, authoritarian educational attitudes prevail, often with very harsh physical penalties.

— Institutionalized children live in a subordinate position. They are a part of a special population rather than individual.

— Juvenile delinquency is very high among institutionalized children.

— Children reared by the state have to leave their institutions when they are 16 years old for an unknown world, without any preparation, supervision or advice.

— There is an increasing aversion towards the institutionalized children by the outside world (Ranschburg, 1990, pp. 5-6).

III. Problems of children related to fiscal austerity and the transition to the market economy

As mentioned in the Introduction to this chapter, the years 1989-91 have been characterized by the introduction of radical economic reforms, though with varying degrees of intensity and according to different timetables, in practically all central and eastern European countries. Efforts at macroeconomic stabilisation, liberalisation and privatisation — often compounded by adverse changes in the international environment — have induced a number of often unavoidable adverse short-term effects which, it is hoped, will be tackled by the safety nets and new social policies being developed (see Chapters 2 and 4). This section will review

the initial evidence on problems affecting children because of the above-mentioned measures. It must be clearly stated, however, that in view of the short time elapsed since the introduction of the reforms, the information presented is, of necessity, limited. In addition, as the economic reforms are still underway, not all the effects have worked through the system. Although a reasonably complete evaluation would probably be possible only in a couple of years time, even at this relatively early stage, a number of warning signs of possible greater deterioration are apparent.

1. Increasing numbers of children living in poor families

The number of children living in poor families was increasing even prior to the present changes (see Part I, Section 1). Shrinking real wages and declining or stagnating social security transfers (see Chapters 3-8) make it very likely that the number of children living in poverty has been increasing since the reforms started in 1989-90. Evidence from Czechoslovakia, where child poverty used to be marginal, shows that in 1989-1990 there was a three- to four-fold increase in the number of children under the poverty line (see Part I, Section, and Chapter 6). High inflation, which was evident in 1990 and expected to accelerate or remain high in most countries in 1991 (see Robinson, 1991, p. 12, and Chapters 5, 7), is bringing more families under the poverty line at a time when unemployment is rapidly increasing in all countries. In Poland, the real wage index dropped by 32 per cent in 1990 compared to 1989 (and was 14% under the average of 1985-87). Government sources show that wage increases compensated for only 45 per cent of price rises on average and 60 per cent during the second half of the year in 1990. The share of food expenditure is above 50 per cent, on average, for the families of those employed, and 60 per cent for pensioners (by way of comparison, 40% of family budget spent on food is regarded as the standard poverty line in the West). After the abolition or reduction of subsidies on rents and utilities, many families fell into arrears with payments causing still unresolved problems. The number of unemployed soared to over 8 per cent of the labour force. Social benefits and other transfers did not increase in real terms (see Chapter 8). The extremely high ratio of social transfers in the personal income of families with children in the lower income groups in Hungary (over 82% in the lowest 5% income group for families with three or more children and well over 50% for families with two children in the lowest 20% income group — see Chapter 7, Table 7.4) indicates and predicts a substantial risk for children to fall under the poverty line (41% of all poor are already children) if the observed decline in the real value of these transfers continues or the parents lose their job.

According to the federal government of Yugoslavia, the 280,000

persons who had already received regular social assistance in 1989 because of their low income are only the fraction of those in urgent need. The figure of socially-at-risk persons went up to almost 2 million as the consequence of the crisis and fiscal austerity in 1990. Of this very high figure (8% of the population), 1 million are children (Todorovic, 1990).

2. Decline in dietary standards

It is difficult to judge accurately the decline in dietary standards. Deterioration is apparent both in terms of quantity for marginal groups and quality for the mainstream of society.

a) Soup-kitchens, organized by domestic and international charities and government organizations, have re-emerged in Poland and Hungary to provide a daily meal free of charge for the most needy. In both countries these kitchens work on full-capacity catering for predominantly very old people on low pensions, the homeless, and, in Hungary, for a large number of refugees [18].

b) As was mentioned earlier (Part I, Section 3), milk consumption was already reduced in Yugoslavia, where healthy and nutritious food is less accessible for poor children than previously (Todorovic, 1990), and in Hungary (by 16% in 1989-90). In Poland, a 30 per cent decline in milk consumption was recorded in early 1990 as subsidies were cut (Jolly, 1990), along with the increase of the very high share of food expenditure in family budgets. Gradual and rather intangible declines in the dietary standards of children in average families (both at home and in school) are difficult to detect at present. A Polish study concluded in this respect that "...protein deficiency is not a mass problem for Polish children right now. But the likelihood of such deficiency is there in connection with the growing number of poor families, especially families with many children" (ZG TPD, 1990, p. 8). If Poland, after a long crisis and an especially strong 'shock therapy', could manage to maintain dietary standards within acceptable limits, it may be hoped that the situation would not be worse in central and eastern Europe as a whole. However, removing food subsidies without full compensation is on the agenda in most countries as part of the transition. As was shown in the example of the level and composition of the consumption of the poor in the Soviet Union (see Table 1.3), there may very easily be a worse situation in the years ahead.

3. Reduction in enrolment rates in pre-school education as fees are applied or increased

Kindergarten enrolment is voluntary and therefore parents can withdraw their children from them if they cannot pay higher fees for tuition.

Dropping out of pre-school education may create a disadvantage for children both currently and when they enter elementary school. Failure to stop this tendency may contribute to the reproduction of poverty in society. Again, the example of Poland, where kindergarten fees were substantially increased and reached 15-20 per cent of family income in 1990 for families with two children in kindergarten (Jolly, 1990), is the most telling. In May 1990, about 880,000 children applied for admission to kindergartens compared to more than 1 million a year before. The reasons are multiple: (1) the increase in fees for tuition or for school meals — and the growing number of families in financial difficulty; (2) the growing number unemployed mothers; (3) the closure of kindergartens by some enterprises striving for economic efficiency; (4) the closure of some public kindergartens by local authorities unable to finance their operations anymore. Cost saving and 'rationalization' resulted in the reduction in the range of food provision services by kindergartens. Now many of them serve only two meals instead of the earlier three; and in some, particularly in rural areas, children are not served meals at all. At present (April 1991) it seems that an estimated 10 per cent of kindergarten children from the poorest families would require financial help in order to keep them in school (ZG TPD, 1990). This trend is expected to worsen in 1991 (see Chapter 8). In 1990, kindergarten fees were raised in Czechoslovakia as well (Struk, 1990). In Hungary, fees for kindergarten meals would be increasingly a problem for parents with many children if there were not compensations by differentiated rates (Ranschburg, 1990). A short-term crisis is in the offing for 1991 in Hungary as a consequence of the shift in the financing of education to local governments with limited resources. If central austerity plans remain uncompromising and local taxes fail to raise enough funds, many local governments may be forced to close the kindergarten (see Chapter 7).

In Yugoslavia, the situation is different but not less dramatic. Before the crisis, only 20 per cent of children had access to kindergartens (see Part I, Section 5). However, there is now a strong pressure to redirect public funds from financing kindergartens to child benefits in cash to the most needy, noting that "...at a time of crisis, priority should be accorded... primarily to child allowances which reach the family directly and do not involve any major administrative cost" (Todorovic, 1990). In this way, however, public pre-school education in Yugoslavia may disappear altogether.

4. Decline in availability of school books and teaching aids

Subsidies for school books and other teaching aids, once provided free of charge or at a nominal fee, are being cut as part of the economic reforms.

The most radical changes happened, once again, in Poland. In 1990, in-school textbook distribution ceased and pupils had to buy them at retail prices which had, in the meantime, increased because of the liberalisation of the price of paper. This increased textbook prices by a factor of between five and ten and has imposed a heavy burden on families. It is estimated that the yearly cost of school books for a child in primary education was equal to an average monthly salary in Poland in 1990 (Jolly, 1990). The situation is the same with other teaching aids, especially with computers, television sets, videos, or language laboratories which were already almost absent from Polish schools (ZG TPD, 1990). The situation is similar in Hungary, though to a lesser extent (Ranschburg, 1990). In Yugoslavia, the share of those pupils who received their textbooks free of charge decreased from 29 per cent to a mere 6 per cent during the last decade (Todorovic, 1990). In Czechoslovakia, so far subsidies to textbooks were not cut and nor were their prices raised, but there are indications that this policy will change in 1991 (see Chapter 6). In view of the potentially negative impact of shortages of books on the cognitive development of children, the situation needs to be closely monitored.

5. Reduction in access to publicly supported summer camps

Publicly supported summer camps, perhaps, suffered the most dramatic changes in 1990. These camps are extremely important in view of high levels of environmental pollution in many countries in central and eastern Europe. Prior to the political changes, summer camps for children in most countries were organized and subsidised by Communist youth organizations, such as the Pioneer movements. The fall of Party-State structures left youth camps virtually empty in the Summer of 1990 in Hungary and in Romania (Ranschburg, 1990; Radulian, 1990). Organisations such as the scouts are being re-created but are not able to take over this function fully. The intentions of the governments are not clear in this domain. In Poland, where there were more channels for publicly supported recreational facilities for children, the fall, although considerable, is not that drastic. However, there was a 26 per cent fall in the number of children participating in organized summer holidays during the crisis years of 1980 and 1989 (the number decreased from 7 to 5.2 million). In the case of camps, the fall was 39 per cent and in the case of daily summer play centres 52 per cent (ZG TPD, 1990). A remarkable decrease was observed in the number of children sent to summer holiday camps in Yugoslavia as well (Todorovic, 1990). In Czechoslovakia, where considerations about the negative impact of environmental pollution made the public and the government especially conscious of the importance of summer camps, they were continued during 1990 (Struk, 1990).

6. The availability of imported medicine for children

Central and eastern European countries have traditionally been dependent on imports of certain drugs and, in particular, on milk substitutes, insulin, PKU, special foods for allergic children, etc. This dependency is dangerous when shortage of hard currency restrains imports and when drastic, if necessary, devaluation of the exchange rate increases up to five times the domestic cost of such key imports. Deterioration of intra-CMEA economic relations, the shift to a hard currency basis and the decentralization of former pharmaceutical monopolies may further aggravate the medical supply situation for children in 1991 (Struk, 1990). In early 1991, widespread temporary shortages of various medicines were reported in Hungary. In Bulgaria, there is a crisis in infant food supplies (Valchev, 1990). In Poland, the supply of modified or single-component insulin and syringes were critical in 1990 (ZG TPD, 1990). This is extremely dangerous in view of low levels of breastfeeding in these countries. In the case of Bulgaria, the only existing plant producing milk powder (covering less than one-half of total needs) may be closed for technical reasons.

Importing the latest medical instruments and equipment for children seems to be more difficult because urgent needs are most difficult to identify. Clearly all countries in central and eastern Europe are in a critical situation in this field and possible solutions are not yet on the horizon. It is not only a question of modernizing mostly outdated facilities, but mere maintenance may be endangered by budget cuts or lack of hard currency which may exacerbate problems related to the reduction of neonatal mortality.

7. Unemployment and youth unemployment

Children can be hit by unemployment in two ways. First, if their parents lose their jobs and thus the means to support the family; second, if young people about to enter the job market have to stay idle. Unemployment seems to be the single biggest challenge to the well-being of children in central and eastern Europe as there is a large 'hidden unemployment' likely to be unleashed by industrial restructuring, and because in central and eastern Europe wages reflect a carefully calculated two-wage-earner model. Losing one or the only salary immediately brings many families below the poverty line despite the implementation of unemployment benefit schemes in 1989-91. Unemployment figures are already high in Poland, Yugoslavia, and certain parts of the Soviet Union. Crisis, transition and demographic factors are likely to produce dramatic youth unemployment by 1992-95 if the number of workplaces and jobs continues to

contract. In all central and eastern European countries, there was a 2- to 4-year baby-boom during the mid-1970s (Wynnyczuk, 1990, pp. 5-6). These children are entering the labour force in the early 1990s. In Hungary, for example, the number of school leavers will grow from 128,000 in 1990 to 160,000 in 1993, while the number of retirements will remain steady even if the planned five-year increase in retirement age is postponed. The compression of wages induced by the transition tends to increase labour supply further in a period when the demand for labour is likely to be reduced due to protracted restructuring (Andorka, *et al.*, 1990, pp. 259-71).

In Yugoslavia, where there has always been open unemployment, two-thirds of present day school leavers will have to wait, on average, between three to five years before getting an adequate job (Todorovic, 1990, p. 12). Already 70 per cent of registered unemployed are young (Parun-Kolin, 1991). In the Soviet Union, there are 6 million unemployed youth in central Asia and Kazakhstan alone — even before any large-scale restructuring is undertaken (Riazantsev, 1990).

The rise of unemployment was particularly sudden and steep in Poland where, in January 1990, about 55,000 people were out of work and, by January 1991, the figure had risen to 1.1 million (or 8.1% of the labour force). In Czechoslovakia, where full-scale 'shock therapy' is not on the agenda and where unemployment is not yet significant (less than 1% in January 1991), concurring ministries put the estimated figures at 4-6 per cent or 8-10 per cent respectively [19] (see Chapter 6). In Bulgaria, at the end of 1990, there were 70,000 registered unemployed (1.3%) which is estimated to rise to 300,000 (8%) by the end of 1991. In Hungary, unemployment increased rapidly in the second half of 1990, reaching 103,000 by February 1991 (more than 2% of the workforce, but up to 6% in depressed areas).

Unemployment benefit schemes have been implemented practically in all central and eastern European countries. However, coverage for school-leavers, the level, and duration of the schemes are encountering problems everywhere.

8. Deterioration of the housing situation and growing homelessness

A substantial deterioration in the housing conditions of vulnerable groups can be seen in central and eastern Europe. In Hungary, utilities have been disconnected as a consequence of the inability of families to pay increased charges. The number of people who have lost their home is growing rapidly as well [20]. The deterioration is due mainly to the following reasons linked to the crisis: a) the accelerating pullout by the state from the

construction sector; b) a drastic reduction in overall residential construction activities; c) increased financial burdens related to mortgages; d) privatisation of the public housing stock and increased rents and charges for utilities.

a) As one of the first indicators of the crisis in public finances, the share of public sector construction activities started to contract in virtually all countries of central and eastern Europe during the 1980s. The removal of construction subsidies has accelerated the decline in the supply of public housing.

b) In Hungary, construction has been steadily declining since 1986 and it went down by 15 per cent in 1990 alone [21]. The same tendencies can be observed in Czechoslovakia where there was a 30 per cent drop in total construction of flats during the last decade (SEV, 1989, p. 180). In the Soviet Union, the already great housing shortages are further exacerbated by the repatriation of military forces from central and eastern Europe and Germany. It appears throughout central and eastern Europe that private activities have not been able to offset adequately the decline in public construction activities. Pulling out of construction to the extent that the public sector did in Hungary will leave the state with little means for corrective measures, especially when the existing public housing stock is privatized.

c) State subsidies on low interest loans to support private construction were cut, as the burden for the state budget had become unmanageable due to the acceleration of inflation. In Hungary, for example, mortgage subsidies became a major source of financial instability in the budget in 1990. Mortgages were serviced at 0-3 per cent rates for three consecutive years when inflation was running at two-digit figures. In 1991, mortgage rates were raised to market levels *ex post* with a certain graduation or a reduction in the amount of repayable loans. While this solution tends to favour the better off, many poor families face the prospect of losing their flat (see Chapter 7). New loans have already been running at market rates (28-34%), making construction unaffordable for many young families. In 1990, for the first time, a mortgage subsidy appeared in the Bulgarian budget as a sizeable item. There is little doubt that in 1991 the 2 per cent mortgage rates will create the same problems as in Hungary with a forecast inflation rate of 100 per cent (see Chapter 5).

d) Privatization of (run-down) public housing stock may free some funds which could be used to provide some limited support for the needy. These funds, however, are insufficient to compensate for the decline in subsidies for the upkeep of public housing and for rent increases. In private housing markets, flats tend to be rented out at rates above the average total income of young families or pensioners who cannot afford them.

It is difficult, at this stage, to see how social policy can effectively protect vulnerable groups in the population from losing their homes. In those countries where new concepts of housing are being discussed or implemented, market principles prevail (Bulgaria, Hungary, Czechoslovakia, Poland). Token rents in public apartments are being increased drastically at the same time as the prices of all utilities (water, electricity, heating, sewage, garbage collection, etc.) are going up. This is in keeping with the general direction of the transition inasmuch as it reflects scarcity and effective demand in allocation, but does not answer adequately the question of the increasing number of families unable to enter or remain in this market.

9. An air of desperation...

The protracted crises and the expected shocks in the years ahead will definitely impose an increasing psychological burden on already worn out populations in central and eastern Europe. International experiences show that adjustment efforts imply substantial costs in this area as well (Brenner, 1987; Cornia, 1987; Jolly, 1984; Raczynski, 1985). The path of transition seems to be paved by increasing frustration and sacrifice — parents working even longer hours and achieving still less; fathers going abroad to work temporarily or for good; new risks and realities with great uncertainties — and all are likely to take a toll on children. At certain historic moments, challenges of this magnitude may strengthen family cohesion. There is good reason to suspect that this effect will play only a minor role, if at all, in central and eastern Europe. The family structure in this region of Europe is sick and shock therapy is not likely to heal it. The 'air of desperation' may result in even more premature deaths of parents, family tensions and divorces, abandoned children and delinquent youth. All this can have an effect on the well-being, school performance and emotional stability of children. Social policymakers have little time indeed to prepare for this challenge.

NOTES

[1] This chapter heavily draws on national reports on the status of children which were sponsored by UNICEF/ICDC from the following countries: Bulgaria (Valchev, 1990), Czechoslovakia (Struk, 1990), Hungary (Ranschburg, 1990), Poland (ZG TPD, 1990), Romania (Radulian, 1990), the USSR (Labetsky, 1990 and Riazantsev, 1990), Yugoslavia (Todorovic, 1990). I am grateful to the authors of these reports for their work and to

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[2] The best rates for 'frontier countries' were the following: in 1960: IMR: Sweden 16, U5MR: Sweden 20; in 1980: IMR: Japan 4, U5MR: Japan 6.

[3] In Hungary in 1988, more than 80 per cent of infant deaths occurred in the first 28 days of life and almost 2/3 of them during the first week during the time that moters and children usually spend in hospital under medical supervision (KSH, 1989, p. 276).

[4] The median of low birth-weight babies was 7 per thousand for CEE countries (5 in the OECD countries) in the 1980s (World Bank, 1990, p. 219; UNDP, 1990, p. 147).

[5] Maternal mortality in central and eastern Europe is alarmingly high. Between 1980-87 the rates were as follows: Bulgaria 13, Czechoslovakia 10, Hungary 26, Poland 11, Romania 150, USSR 48, Yugoslavia 22 (the OECD median was 8) (UNICEF, 1991, p. 115). The tragically high Romanian figure is expected to fall dramatically when the new abortion law and an improved supply of contraceptives take effect and counter the legacy of former Draconian pro-natalist regulations (Pierotti, 1990, p. 1).

[6] *Komsomolskaya Pravda*, 25 April 1990, gave a detailed account of extreme problems in Turkmenia. In English, see *Moscow News*, No. 26, 1990.

[7] Information on the devastation of Katowice district is based on documents attached to an appeal to WHO and UNICEF by the Polish Ecological Club on 14 March 1990 and on Duch, 1990, pp. 346-7, and Norska-Borówka, 1990.

[8] The former secret military town north of Cheljabynsk in Siberia drew international attention because of lakes which were seriously contaminated by radioactiv contents and which threatened to flood large parts of the area (see *European*, 30 September 1990).

[9] In some parts of the town of Bytom, where a foundry emits 12-46 times above the norm cadmium, lead and zinc, IMR increased from 32 per thousand in 1986 to 52 per thousand in 1989 (Norska-Borówka, 1990, p. 1393).

[10] It should be noted that price and income elasticities work differently in a shortage economy. If meat is always in short supply and partially rationed, or distributed through special shops for the privileged, then the planners are forced to substitute meat for dairy products. Free markets, where and when they existed, were usully beyond the reach of low income groups.

[11] Milk consumption declined from 125.6 to 102.6 litres per capita between 1970 and 1986, according to Yugoslav statistics (Todorovic, 1990, p. 3).

[12] *Népszabadság*, 1 February, 1991.

[13] Indeed Romania, Bulgaria, Poland and Yugoslavia have lower divorce rates than any other European country except for Switzerland (Wynnyczuk, 1990, p. 22).

[14] The Bulgarian national status report included in this category all children born out of wedlock or living with single parents (17.6%), temporarily separated parents (0.8%), having alcoholic or mentally ill parents (3.1%), and other partially or fully institutionalized children (10%) (Valchev, 1990, p. 5).

[15] In the United States, the number of juvenile delinquency cases increased steadily between 1960-80 from 2 to 4.5 per 100 youth and declined slightly to 4.3 in 1983 (Cherlin, 1988, p. 139). In the United Kingdom, there was a 27 per cent drop in the number of juveniles (10-16) sentenced or cautioned for indictable offences between 1979 and 1988. Part of this decline may be accounted for by the decrease in the population of this age group, and also the decline in criminality in the second half of the 1980s. The number per 100 rose from 2.9 in 1979 to 3.6 in 1985 and fell back to 3.0 in 1987 (Bradshaw, 1990, p. 41; Griffin, 1989, p. 190).

[16] In the United States, the rate of use of marijuana among 12- to 17-year-old children was 12 per cent in the first half of 1980s, a marked decline from the peak of 16 per cent in 1979. In 1984, however, 40 per cent of high school students still used marijuana and more than 50 per cent were exposed to illicit drugs (Cherlin, 1988, pp. 137-8). The impact of the

entry of relatively cheap and particularly damaging crack has not yet been accounted for. In the United Kingdom, 3-5 per cent of 15-year-olds are thought to have used solvents (Bradshaw, 1990, p. 40).

[17] All figures here refer to the child population under 16 years old. National practices in accounting for institutionalized children vary, therefore the numbers are not yet strictly comparable - despite international efforts to standardize them (Himes, 1991).

[18] *Magyar Nemzet*, 24 April 1990; *Népszava*, 4 March 1991.

[19] *Financial Times*, 6 February 1991.

[20] According to some estimates, the number of homeless people in Hungary was between 25-30,000 in 1990 (*Magyar Nemzet*, 29 September 1990). In another article, inwhich a pregnant homeless mother was interviewed, a more radical estimate put their number at around 50,000 (*168 Ora*, 2 October 1990). An occupational sit-in strike of hundreds of homeless people in the Southern Railway Station in Budapest first drew the attention of the public to this problem during the winter of 1989-90. A temporary solution to the problem was found then, but it may prove to be a recurrent issue as the situation deteriorates (Andorka, *et al.*, 1990, pp. 440-4).

[21] *Magyar Nemzet*, 2 March 1991.

CHAPTER 2

WELFARE STATE MODELS IN OECD COUNTRIES: AN ANALYSIS FOR THE DEBATE IN CENTRAL AND EASTERN EUROPE

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Introduction

The introduction of markets, and changes in the role of the public sector in central and eastern Europe, will have major implications for social policy. Reform is therefore inevitable. This chapter does not offer specific suggestions for the reform of social policy in central and eastern Europe, but examines three different kinds of welfare states in OECD countries in the hope that their diversity of social policy experiences may help to shed light in our part of Europe.

Section I describes the policy instruments which are used in western welfare states, focusing on the five 'pillars' (i.e., (i) pensions and survivor benefits, (ii) health care, sickness and disability transfers, (iii) family benefits, (iv) social assistance, and (v) unemployment support) and the problems associated with them. Clearly, some of these instruments have also been applied in the central and eastern European welfare states; social insurance is a notable example [1]. But others are hallmarks of market economies, including private market provision and the use of personal income taxation in conjunction with other instruments. Furthermore, an instrument such as social insurance, which has been used in formerly centrally-planned economies, may take on a different role in a market economy; this paper describes how, when compared to alternatives, social insurance may provide positive economic stimuli for market economies.

Section II describes three broad models of social policy provision in three countries which typify them — namely, the *Modern Liberal* (the United States), the *Social Democratic* (Sweden) and the *Modern Conservative* (the former West Germany). Section III presents an overall if not exhaustive comparison of the operation of these three welfare states by looking at aggregate statistics of their cost (as a percentage of GDP) and of their performance in alleviating poverty (especially among children and the aged). Some general observations conclude the study.

Finally, a warning. The welfare states in the OECD area relate to economies which differ from those in central and eastern Europe on several accounts. To start with, their level of development is much higher. Per capita GDP in the eastern European countries (including the USSR) in 1990 was estimated to be little more than a quarter of that in market economies (ILO, 1989, p. 6).

In addition, the structure of employment is quite different; the employment in agriculture is less than 5 per cent in all three OECD countries considered, compared with a share which ranges, in central and eastern Europe, between 12 per cent in Czechoslovakia and 30 per cent in Romania (ILO, 1989, p. 17). It has long been recognised that social insurance is less appropriate in countries where there is a large self-employed agricultural labour force (the future ownership structure of collectivized European agriculture is an important issue here). The welfare states of OECD countries in the 1950s, when their economies were more akin in terms of level of development to those currently existing in central and eastern Europe, would certainly be worthy of study but this goes beyond the scope of this paper [23]. But then one would have to consider differences in demographic structure between post-war OECD countries and present-day central and eastern Europe (the importance of demographic structure as a determinant of welfare state expenditure is underlined in Section III). Moreover, the urgency of reform in present day eastern Europe may preclude the kind of gradual development of the welfare state that occurred in OECD countries in the 1950s, while the initial differences in terms of existing institutions and degrees of inequality would have to be taken into account.

I. Social policy instruments in western market economies

Some instruments of social policy have been used both in the East and West; in particular, social insurance has been important in both. However, we need to clarify their role in market economies. We exclude consideration of price subsidies (which have been of particular importance in the former centrally planned economies).

1. Public sector support in cash and kind: some definitions

Social insurance benefits depend on previous employment history and in general are independent of a claimant's personal or family income. Benefits are financed from contributions which may be levied on any combination of workers, employers and the state, but an individual's benefit is not, in most cases, related actuarially to contributions. Typically, social insurance benefits are not paid from an accumulated fund of past contri-

butions, but on a "pay-as-you-go" (PAYGO) basis: today's contributors pay for the benefits of today's beneficiaries. This has important implications when the ratio of contributors to beneficiaries changes, as discussed in Section III. In the case of unemployment and sickness, eligibility for social insurance is typically of limited duration.

Means-tested benefits are more prevalent in OECD economies than in central and eastern Europe; means-testing can even be considered as a hallmark of some OECD welfare states. These benefits do not, in general, depend on the employment or contribution record, but are assessed on the basis of the income and needs of the claimant's household. They are typically of indefinite duration, payable as long as need is demonstrated. Their finance falls exclusively on public revenues.

Universal benefits are made available to people independent of employment record or income. They may be in cash, such as family allowances, or in kind, as with the provision of 'free' health care. They are usually financed by general tax revenue.

2. Differences in income support and economic impact

These three types of social policy differ in their role for *income support*. Since means-testing takes into account other family income, the benefits will, on average, provide a lower level of income than either social insurance or universal benefits. The targeting of benefits to the needy may help save on scarce public resources. Yet, the administrative cost involved in means-testing tends to be high. Means-tested benefits are restricted to those in need, but their coverage may not be complete for this group since means-tested benefits often have low levels of take-up; some people do not claim the benefits to which they are entitled because of ignorance of the procedures, or because of the stigma associated with a close inspection of their family's finances. In the United Kingdom, it has been estimated that, in 1983-4, little more than half of those entitled to means-tested assistance payable to employed family heads on low income claimed their entitlement (Department of Social Security, 1988, Table 48.02). In the United States, the take-up rate of means-tested assistance for the elderly in 1974 was also only about 50 per cent (Warlick, 1982).

Social insurance benefits may also have coverage problems, in this case due to the need to have an appropriate employment or contribution record, or to limited duration of entitlement. For example, only one in five of those claiming unemployment benefits in Britain in November 1989 were receiving unemployment insurance (Micklewright, 1990).

The different benefit systems are also distinctive from an *economic* standpoint. Consider the differences in financing between means-tested benefits and social insurance. Social insurance contributions may in-

fluence employers' lay-off policies; this may be manipulated by relating employers' contributions to lay-off behaviour (e.g., Topel, 1983). The same applies to workers' behaviour; for example, the provision of social insurance during unemployment provides an incentive to enter the labour force.

Social insurance is likely to influence the choice of sector in which to work. It gives an incentive to enter covered employment in the legal economy, rather than self-employment or the illegal economy where social insurance coverage does not exist (Atkinson and Micklewright, 1990). In contrast to means-tested schemes, social insurance does not generally have negative implications for family labour supply and household savings. Means-testing results in high implicit marginal tax rates on the labour supply of the claimant's family; the earnings of a claimant's family may be 'taxed' up to a rate of 100 per cent when the benefit is reduced, dollar for dollar, against other family income. In the same way, means-testing may discourage saving since assets, or the income derived from assets, are typically taken into account in the benefit calculation. In brief, the economic impact of social insurance may be positive when compared to a means-tested alternative.

These different economic effects arise due to the different incentives the schemes may present to benefit claimants, to their families, and to their employers. And, in market economies where economic agents have greater freedom of choice, the different incentive-effects are likely to have a greater impact than would be the case in centrally planned economies: people may decide whether to participate in the labour force, instead of being obliged to do so; firms may choose whether to lay off workers or not[4]. The introduction of markets into formerly centrally planned economies should therefore alter the economic impacts of pre-existing social policies. The same applies to the social impact; when people were obliged to work, and work was always available, then the problem of low benefit coverage in social insurance schemes due to a bad employment history was less of an issue.

3. Private provision

We can distinguish three major types of private sector arrangements. First, individual insurance contracts (such as life insurance); second, group and occupational insurance plans (such as company health plans and occupational pensions); and, third, charitable organizations and voluntary philanthropy[5]. Among the three, the second is by far the most common and financially important in OECD countries. In the United States, for example, occupational pension plans account for 80 per cent of total private pension expenditure (Esping-Andersen, 1990, p. 84), and about

four-fifths of private health insurance is also related to the employment contract (Barr, 1990, p. 106).

The debate over the pros and cons of private provision is complex, and a proper analysis would require a more detailed (and analytical) treatment of the issues than there is room for here (see Barr, 1990, for further discussion). Only the most important issues for the debate in central and eastern Europe are discussed in this study.

First, the public sector welfare state exists, in part, because the private sector *cannot* provide adequate insurance for all individuals against the risks of low income in old age, sickness, unemployment and disability; there exists what is known in the economic literature as 'market failure'. Since market failure implies that a complete private market for the insurable risk does not exist, it is *efficient* for the public sector to step in. This is one of the classic arguments in favour of social insurance (e.g., Diamond, 1977; Creedy and Disney, 1985; Barr, 1990) [6]. The public-private debate is not simply a case of the economic efficiency arguments of private provision, on the one hand, being balanced by equity considerations leading to a public sector welfare state, on the other.

Market failure may come about for a variety of reasons; private insurers may be unable to assess risks, such as the risk of future inflation eroding pension entitlement [7]; they may be unable to offer insurance at affordable premia, as in the case of insurance against unemployment for low-paid, unskilled workers; individuals' risk probabilities may be interdependent, implying that there may be periods when there are too many losers to be compensated [8]. There are other valid reasons for public provision of social protection, including redistribution and paternalism (myopia may lead to inadequate saving by individuals). But, in light of the introduction of a market system in eastern Europe, *market failure* must be one of the most important considerations; public provision may be justified on the grounds of economic efficiency [9].

Second, the causality between public and private sectors may run in the opposite direction. Gaps in public social security catalyse a demand for private sector alternatives. This is best illustrated by contrasting Sweden and the United States. The comprehensive and generous Swedish welfare state means that pressures for private alternatives or supplements are marginal, and in practice limited to a small occupational pension sector of no real financial significance. In the United States, by contrast, there is a very large private health, sickness and pension insurance industry. Some might argue that it is so large precisely because the American market is *more* efficient than elsewhere, i.e., that it 'fails' less often. This would imply that public sector provision in the United States does not need to be so great since the private sector has done the job well. But this position is indefensible. Were the U.S. social security pensions more generous, or

were its public health care system to provide better coverage (see Section III), it seems inconceivable that the private sector would be so well-developed.

Third, the private insurance sector caters primarily to the more privileged sections of society; private plans are distributed quite unevenly across the economy. While they can function in large firms with stable production, manpower and sales profiles, they are difficult to introduce in small firms, in the services sector, and in areas that depend on a flexible workforce. In the United States, in 1983, 82 per cent of employees working for an employer with a staff of 500 or more were eligible for their employer's occupational pension plan, compared to only 23 per cent in firms with less than 100 employees (Bodie, 1990, p. 36). It is also the case, especially in Europe, that private plans cater mainly to higher level company staff (managers and executives), and less to the average manual or clerical worker. As fringe benefits, private plans often serve to reward loyal employees, or to add non-taxable benefits to the salary. More marginal groups, such as temporarily and seasonally employed, the recurrently unemployed, single mothers, inactive persons or widows, are unlikely to have private insurance cover. Lack of public provision will not therefore necessarily create private provision. This we know from the pre-war United States where the essentially complete absence of any public social security failed to stimulate private protection despite government inducements. In part, the explanation has to do with weak purchasing power among workers (a market failure argument, as above); in part with the weakness of trade unions in collective bargaining, and with volatile capital markets. In this instance, both the market *and* the public sector have failed.

Market failure means that it may be *more* efficient for the public sector to provide social protection. It is frequently argued that welfare states are a source of economic inefficiency: cash benefits may distort labour supply decisions, and public social services may not easily be subjected to cost controls. Against these arguments, it is held that work incentives are unlikely to be affected seriously; that social security may actually improve productivity since workers will be healthier, more productive, and less resistant to economic change; that private sector alternatives may indeed be more costly since they will multiply administrative tasks [10]; that inefficiency and cost inflation will exist in private sector supply if the industries are monopolistic or oligopolistic. Again, this literature is too large for us to address here (some of it is reviewed in Danziger, *et al.*, 1981; Atkinson, 1987). However, it should be noted that a weakness of the debate is its tendency to treat public social security as a homogenous entity, while it is obvious that different types of provision may have different economic impacts. As stated earlier, the effects of

social insurance may be different, but also more beneficial than those of means-tested benefits ".

4. Tax expenditures and the tax system

The tax system represents an important instrument of OECD welfare states, the personal income tax in particular. Like the introduction of private markets, this is largely a new player for central and eastern European countries, where there is little experience of personal income taxation.

Personal income tax has played a major role in complementing private sector provision in OECD countries, mainly by granting a tax relief to private health and pension contributions. Since this is, in effect, a subsidy, it is usually labeled a 'tax expenditure'.

The existence of tax expenditures in OECD private insurance markets means that it is difficult to regard this sector as purely private. In any event, a substantial tax expenditure subsidy certainly implies that private sector insurance is not the result of the independent free market. The size of the implicit public sector subsidy can be very substantial: the value of tax expenditures for private pensions in the United States in 1981 was equal to nearly 20 per cent of total public pension expenditure; a similar figure applies to health, the bulk of this being subsidies to employer health plans (OECD, 1984, p. 82).

But the tax system has a far bigger role to play than just that of encouraging private sector provision. Tax allowances on income may be granted directly to individuals, and these can be varied with age and family status or other characteristics, such as disability. Consider the case of family allowances. A personal tax system allows a government to reduce their value to higher income recipients by making it subject to tax, thus countering the criticism that universal benefits are wasteful because they provide transfers to the rich as well as to the poor. Alternatively, tax allowances could be given to persons with children in place of a universal benefit (with some modifications, this is what happens in the U.S.). We are not necessarily advocating either of these policies (the former is progressive, the latter regressive); we mention them purely to illustrate the wider menu of policy instruments that a market economy will introduce in central and eastern Europe.

5. Active labour market policy

In an industrialised market economy, income for the great majority of people comes first from work, either directly or indirectly via pension entitlements linked to past employment history. A major function of the

welfare state is to provide a cash benefit to those without adequate work-based income. Alternatively, or additionally, the state may try to improve people's employment prospects, and thus their income position. This is what we mean by 'active' labour market policy. It includes government employment agencies, training schemes for the unemployed and other groups, measures to support labour mobility, subsidised jobs (sometimes for particular groups such as the disabled), and direct job creation.

Any discussion of welfare state policy in a market economy has to consider active labour market policy, not least due to the prominence of the problem of unemployment in market economies. In the short term, its impact on income may be just as great as that of cash transfers; the provision of sheltered employment may give a higher income to a disabled person than a disability benefit. In the long term, the effect of active labor market policy may be profound; the principal aim of training schemes for the unemployed is to give them the skills to secure employment and remove themselves from what may be a cycle of unemployment, unstable work, and welfare state dependency. To put it differently, the costs associated with active labor market policies may result in huge savings elsewhere, such as in unemployment compensation or social assistance. They may also have an economic dividend to the extent that active labor market measures reduce the waste of manpower resources.

II. Three welfare state regimes

The OECD countries differ considerably in their mix of social insurance, means-tested and universal benefits, in the extent of private or market provision, in the granting of tax expenditures, in their use of active labour market policy, and in the application of other instruments which we have not considered, such as price subsidies. In this section three different welfare state models are examined: the modern liberal state (the U.S.A.), the social democratic state (Sweden) and the modern conservative state (West Germany). The aim is to give an overall picture of each system, not to provide an exhaustive analysis [12].

The initial development of social policy differed sharply among the industrial capitalist countries, differences that can be seen reproduced in today's western welfare states. From the late 19th century until about the 1930s, we can distinguish two contrasting models. First, in the liberal regimes like Scandinavia and the Anglo-Saxon New World, the response was to upgrade traditional poor relief systems and to encourage private solutions. This approach conformed closely to the ideals of classical liberal political economy: stringent means-tests and meagre benefits would assure that public benefits would go only to the demonstrably needy, would not

weaken the work-incentive, and would not burden the public budget.

The second historical model is the Continental European emphasis on compulsory social insurance, first launched by Bismarck in the 1880s. This envisaged a strong and direct state role, mainly in stipulating compulsory membership and setting standards; it favoured social insurance programmes which were occupationally and status-distinct, and administered autonomously by the relevant corporate agents. These principles closely mirrored the reigning paternalistic, etatist, and conservative political economy that guided the rise of capitalist industrialization in nations such as Austria, France, and Germany.

Today's OECD welfare states spring from the various ways in which adaptations and reforms were undertaken on the basis of these two original models. Three sharply distinctive contemporary welfare state regimes can be distinguished: the first group consists of the countries that only marginally reformed the traditional liberal social assistance model. In this group, means-testing remains a dominant principle in what Richard Titmuss (1974) called the 'residual welfare state'; our example here is the United States but others are Australia and Canada.

1. The modern liberal model: the United States

The continued residualism in the United States regime is best illustrated by the programmes excluded from social policy. Except in a few states, there is no system of public sickness and maternity benefits; there is no programme of child benefits; and there is no national health plan covering the whole population.

Two comprehensive social insurance schemes do exist. Old-age, Survivors and Disability Insurance (OASDI) covers about 95 per cent of the employed and, in 1988, nearly 60 per cent of beneficiaries aged 65 or older relied on the scheme for at least half of their income (Department of Health and Human Services, 1989, p. 6). An OASDI old-age pension can first be drawn at age 62 (full benefits are payable if retirement is at 65) [13]. Persons attaining age 62 in 1991 or later will require at least 10 years of work in covered employment to be eligible. In 1980, some 87 per cent of those aged 65 or more were in receipt of a social security pension (Esping-Andersen, 1990). The benefit formula is weighted in favour of low earners. Assuming a full worklife, an OASDI pension would pay around 60 per cent of past earnings if employment had been at the Federal minimum wage, 41 per cent for earners at the average wage, and only 27 per cent if employment had been at the maximum amount subject to OASDI contributions (Department of Health and Human Services, 1989:15) a level equal in 1985 to just under twice average earnings in manufacturing (Gordon, 1988, p. 77). The favouring of low earners in the

scheme has been one factor influencing the development of private pensions and, in 1983, 56 per cent of all employees in the United States worked for an employer with an occupational pension plan (Bodie, 1990).

Unemployment insurance (UI) was also introduced in 1935. Organised on a state basis, UI systems display enormous variations (although all states are obliged to have a UI programme). The typical maximum duration for benefits of six months is low by international standards (if state unemployment is unusually high, UI entitlement may be extended by 13 weeks). In 1987, some 30 per cent of claimants exhausted their UI entitlement, although in some high unemployment states the figure was 50 per cent (Department of Health and Human Services, 1989a, Table 8.A2). A combination of the short duration of entitlement, poor employment histories, disqualification for voluntary quitting and less than complete take-up, resulted in fewer than 30 per cent of the unemployed stock (defined on a job search criterion) being in receipt of UI in 1987 (Blank and Card, 1989).

The fate of the unemployed individual with no UI, or with exhausted entitlement, is representative of that of many low income groups in the United States; much less financial assistance can be expected than in many other OECD countries, and the prospect of virtually *no* income from the state is a very real one. The United States has no nationwide means-tested social assistance safety net. Families with children, where the main earner is not employed, may apply for means-tested Aid to Families with Dependent Children (AFDC) [14]. The aged, blind and disabled may apply for means-tested Supplementary Security Income (SSI) [15], but the only nationwide means-tested scheme open to all is Food Stamps which subsidizes food purchases [16]. State or local level means-tested schemes (known as General Assistance) may provide some sort of safety net for the needy, but these are extremely varied.

The situation of health care is not dissimilar. In-patient hospital bills and home-care services for the aged are covered by the Medicare programme (minus the first $560 in 1989). The payment of a monthly premium ($31.90 in 1989) secures cover for additional expenses. The Medicaid programme provides means-tested coverage for the non-elderly poor, but there is no national health service or compulsory sickness insurance. It is not therefore surprising that private health insurance has flourished. Notwithstanding the existence of Medicare, even 60 per cent of the elderly in 1979 had private health insurance (Pauly, 1986).

As in most areas of social policy, the U.S. approach to active labour market measures has been limited; for example, there exists no public system of labour exchanges. The CETA (Comprehensive Employment and Training Act) of the Carter Administration was primarily targeted to youth training, but it was almost entirely dismantled during the 1980s.

The United States spends far less on active labour market policy, as a percentage of GDP, than the other two countries. Active measures in the labour market have been used, in part, to police cash transfer schemes, as in the 'workfare' requirement for AFDC (the payment of benefits in return for unskilled work). However, recent policy initiatives have strengthened the training element in AFDC programmes (Gueron, 1990).

For the well-paid, stably employed full-time wage earner who can supplement public social security with private benefits, the U.S. system offers reasonably adequate income security. If he or she has children, there is a generous tax expenditure, in the form of a child tax allowance, equal to that for a single adult (just under $2,000 in 1988) and worth most to the person paying the higher of the two marginal tax rates [17]. But for the unstably employed, single parents, and other marginal groups, the U.S. model is very weak. For such groups, social insurance hardly applies, implying dependence on means-tested assistance in one form or another, or the possibility of virtually no income at all. The child tax allowances are of no use to those with little or no taxable income.

2. The social democratic model: Sweden

The Scandinavian countries form the second group of welfare state regimes for which Sweden shall serve as example. Beginning with a largely liberal social assistance tradition, the evolution of these countries towards a modern welfare state was dominated by social democratic governments. The social democratic model in Sweden is characteristic in many respects. Under the slogan of the "people's home", the principle has been to include the entire population, whether in need or not, under the main areas of social protection. The main goals have been to eradicate poverty and to achieve social solidarity and equality through social policy. The underlying philosophy is that a small, internationally competitive nation must rely on its human resources, and that optimal productivity is best achieved by assuring that individuals and families are guaranteed adequate welfare.

In contrast to the United States, the Swedish welfare state provides a basic guaranteed income with a range of universal benefits, the most important of which are universal child benefits, flat-rate pensions, and health care [18].

The system of child income support relies solely on direct cash transfers (and services); in contrast to the United States (and Germany), there is no use of tax expenditures. In 1985, child benefits for a family with two children equalled 9.4 per cent of the average wage in manufacturing, rising to 25.9 per cent for families with four children. The rate thus rises according to family size (Gordon, 1988, p. 285). Large families

are also more-or-less automatically eligible for housing allowances. The net result is a substantial income redistribution to families. Throughout the range of family policy, the belief is that investment in childhood is the best guarantee against poverty and social costs later in life, as well as an investment in national productivity.

Kamerman and Kahn (1988, p. 358) compared the situation across countries in 1979 for an employed single mother with two children earning half of the average production worker's wage. In Sweden, non-means-tested benefits alone equalled the other half of the average wage, so that the single mother's post-tax net disposable income ended up being 23 per cent higher than the average wage. In the United States, if the same half-time working single mother applied for means-tested AFDC and Food Stamps to supplement her income, then, together with her own earnings, she would have had, in 1979, a disposable income amounting to 69 per cent of an average worker[19]. In other words, the same woman in Sweden would have received, in 1979, double the level of income (relative to the average wage) than she would have received in the United States (and without the need to undergo a means-test). In West Germany, the same person would receive less than a quarter of the wage in non-means-tested benefits and the net disposable income after tax would have equalled 71 per cent of the average wage — about the same level of support as in the United States.

The principle of a universal flat-rate pension in Sweden reflects a commitment to a guaranteed basic citizen's income, but it implies a lower level of income replacement for those on higher earnings. Originally, Swedish pension levels were quite modest; in 1950, the flat-rate pension equalled 20.7 per cent of the average wage, although given its universality, the net income replacement rate for a retired couple would double to 41.4 per cent. With income-tested supplements, the same couple could count on a net replacement rate of 57 per cent. Thus, for an average working family, the universal pension provided a fairly adequate income guarantee from the very start of the scheme; but, for a better-paid salaried employee (earning, say, twice the worker wage), the level of income replacement could be quite low. The result was private pension growth, first among the better paid, and subsequently among average wage earners as prosperity brought steadily rising incomes.

The growing pressures for private supplements provoked the emergence of the earnings-related compensation principle in the state scheme. The social democratic movement feared that the evolution of private occupational plans would undermine the principle of solidarity and universalism and pressed therefore for state provision. An earnings-related second-tier system, dependent on employment history, was therefore added to the pension scheme in 1959[20]. This requires 30 years of covered

employment for a full pension, compared to 40 years in the United States (and 45 years in the German system) and the pension is calculated on the basis of the best 15 years. (Sickness, accident and unemployment benefits all became earnings-related (and taxable) in the 1960s [21]). To boost national savings, this second-tier pension is intended to be fully funded rather than being financed on a PAYGO basis.

To avoid a dualism between those qualifying for earnings-related pensions and those who would receive only the flat-rate pension, the government introduced what might be called 'transfer-tested' supplements for the latter (these people are usually entitled to housing allowances) [22]. The result is that upon retirement, everyone is guaranteed a minimum pension equal to 75 per cent of the average full pension.

The Swedish welfare state model is also distinctive in its attempt to integrate people into the labour market. A high level of employment increases the finances of the welfare state and helps reduce social expenditure burdens. The aim is to boost the individual's (and especially woman's) capacity to harmonize work and family life, and to minimize the amount of time spent unemployed.

First, there are generous maternity (and paternity) leave and child-care provisions designed to secure a high level of female labour force participation. During the first year of childhood, parents may share a full year of paid leave at 90 per cent of net normal earnings. This is paid for by the sickness insurance scheme which, in 1983, was mainly financed by a 9.5 per cent employer payroll tax (Gordon, 1988, p. 299). This contrasts with other countries, such as Germany, where the employer must pay directly a proportion of earnings during maternity leave. The take-up of these leave arrangements is high: on an average working day, nearly 50 per cent of employed women with small children (0-2 years) are not at work (this figure includes holidays) (Esping-Andersen, 1990, p. 155). The cost has — until recently — been argued to be acceptable in light of the opportunities that maternity leave allows women in terms of uninterrupted labour force participation: in 1985, the participation rate of women with infant children was 82 per cent — hardly lower than the male participation rate (Esping-Andersen, 1990, p. 155).

Second, active labour market management is more developed than anywhere else in the OECD, and this has gone hand in hand with an explicit full employment policy. Sweden is famous for its very low unemployment rate throughout the post-war period, and this has been achieved, in part, by high government expenditure on retraining, labour mobility, sheltered employment, and direct job creation. It should be noted that active labour market policy in Sweden is characterized by the "stick" as well as the "carrot". The carrot lies in generous benefits to participants combined with the promise of improved future employment

prospects. The stick is that unemployed workers risk losing their unemployment benefits if they refuse to participate in retraining or alternative employment measures. Unemployment insurance lasts a maximum of 60 weeks (there is a non-means-tested flat-rate benefit for those with insufficient employment records for insurance benefits). For those whose entitlement to unemployment benefits is exhausted, the government provides a *de facto* guarantee of a place in a training scheme or a job programme.

3. The modern conservative model: West Germany

The degree of welfare state reconstruction that has occurred in the modern 'conservative' model is considerably less than in either the liberal or social democratic case. This is not surprising since the social insurance systems had by and large matured by the 1950s. The thrust of post-war West German social reform has been to modernize the traditional social insurance schemes and to establish a safety net for those groups falling outside their protection.

The Christian Democratic Union (CDU) synthesis of the 1950s has come to characterize the contemporary West German welfare state. On the one hand, it stipulated that price stability be given priority over full employment. On the other, it largely reinstated the pre-war social insurance schemes along the traditional occupationally distinct lines.

The CDU model was, however, subject to considerable internal conflict with the neo-liberal wing advocating the privatization of social insurance (with the aim of leaving government with little more than a means-tested assistance programme) and with the Catholic labour wing demanding that the existing system be upgraded. The conflict was resolved in favour of the latter and a string of reforms resulted. The rise of the Social Democratic Party (SDP) in the 1960s and 1970s produced an additional impetus. The result has been a welfare state model that falls in between the extremes represented by Sweden and the United States. This model has implicitly incorporated the principle of a basic minimum, but largely through income-tested social assistance rather than genuine social rights.

In Germany, child benefits constitute one of the few universal social rights. Their level is, however, substantially lower than in Sweden; in 1985, the ratio of family allowances to average manufacturing wages was only about half that of the Swedish system (Gordon, 1988, p. 285). Most other benefits in the German system are provided by employment-linked social insurance.

In the earnings-related pension schemes, "the benefit formula is more strictly related to earnings and years of insurance than those of most other old-age systems" (Gordon, 1988, p. 59). For a full pension, 45 years of

covered employment are required; for a minimum pension, at least 25 years. This is even more restrictive than in the United States (10 years). A minimum level pension after 25 years of covered employment would not produce a very satisfactory level of income: the minimum pension for a couple in 1980 was 635 marks per month, only about half the official social assistance-based poverty line which at that time amounted to 1,200 marks (Kohl, 1990, p. 14). Legislation provides for a special widower benefit and income-tested old-age assistance benefits for persons without insurance entitlements.

The (gross) replacement rate for a single pensioner in Germany (on a full pension) declines from 55 per cent for an average wage worker to 40 per cent for a person with twice his earnings. In Sweden, it would decline from 80 to 60 per cent, and, as already noted, in the United States from about 40 to 27 per cent. Hence, for higher income earners, the German system provides a better level of income replacement than the American one, but a substantially lower one than the Swedish (the Swedish pension system provides the best replacement at both ends of income distribution).

As with pensions, entitlement for unemployment insurance depends on a lengthy employment history, taking into account the seven years prior to unemployment. The duration of entitlement will vary from six months to five years, depending both on previous employment history and the age of the applicant. Those with no insurance benefit, representing as many as 60 per cent of the unemployed in December 1988 (Brunhes and Annandale-Massa, 1989), may apply for means-tested unemployment assistance, which also requires a previous employment requirement. Income support during sickness is also employment related, with employers having to pay the benefit during the initial period. There is compulsory membership of sickness funds; these finance a proportion of health care costs and also partly reimburse employer-paid sickness benefits.

For those without insurance benefits (neither unemployment insurance or assistance in the case of the unemployed), there is, unlike the United States, recourse to a means-tested safety net or *Sozialhilfe* (social assistance). This is administered by local authorities and, although there is some local variation, benefits are provided at federally-determined standard rates. The proportion of all households dependent on social assistance remains quite low, although rising: 2.1 million persons in 1980, 3.1 million by 1987 or about 5 per cent of the population (Backer, *et al.*, 1989, pp. 141-2). This rather sharp rise may be an indication of the weaknesses of the German welfare state when confronting economic stagnation and higher rates of unemployment.

From 1969 onwards, Germany began to develop a range of active manpower measures. As in Sweden, it is administered by an autonomous

public body, but it has been institutionally limited as it is financed by the unemployment insurance system (to which both employers and employees contribute). Hence, with rising unemployment benefit burdens in the 1970s and 1980s, the fiscal scope for active measures was rather circumscribed. Active measures have primarily emphasized vocational training, rather than active employment promotion.

Instead, in order to cope with rising unemployment, the German system sought to reduce labour supply using a combination of the unemployment and pension insurance schemes to induce early retirement, either via the post-1972 flexible retirement law (age 62), or by permitting early retirement for those aged 58 and over who have been unemployed for a year. The results have been dramatic. The employment activity rate of males aged 55-64 fell from 79 per cent in 1970 to 51 per cent in 1985. This compares with the smaller decline in Sweden, from 84 to 73 per cent, and in the United States, from 78 to 64 per cent (Jacobs, Kohli and Rein, 1990, Table 4).

The German welfare state may be said to provide adequate income maintenance protection for the employed person, and this helps explain why the private sector plays only a marginal role. Due to the less adequate pension levels among high-income earners, there exists an important (and growing) niche of private company pensions catering mainly to the upper-level staff. The German welfare state is, however, much less comprehensive for the population excluded from employment, such as widows, single parents, the long-term unemployed and youth unable to find a job.

Summary

Table 2.1 summarizes the principal features of the three models. The Swedish model is characterised by its universalism, egalitarianism, comprehensiveness and its active commitment to full, if not maximum, employment. It is citizenship that constitutes the criterion of eligibility for various benefits and solidarity the criterion of distribution.

The essence of the U.S. model is a limited core of social security (lacking health care, sickness and family programmes), coupled with an emphasis on means-tested targeted benefits to the poor, and reliance on private market provision for the better-paid. It is a residual approach to social security in the sense that government generally refrains from active policies for full employment. In the United States, it is mainly need or ability to pay that constitutes the criterion of eligibility; targeting and market position the criteria of distribution.

The key element of the German model is its construction around the compulsory social insurance system and, as a result, its tendency towards dualism in the treatment between those actively participating in the

labour force and those inactive. A second key element is its (more recent) use of transfer programmes as a means to reduce labour supply — a policy which, in contrast to that of Sweden, diminishes productive employment. In Germany, it is largely employment performance that defines eligibility and status that guides distribution.

TABLE 2.1 *Principal characteristics of three welfare state models*

	Liberal-residual	Conservative	Social democratic
	(United States)	(Germany)	(Sweden)
Basis of rights	need/work	work	citizenship
Distribution principle	targeting	occupation/status	universalism
Organization principle	assistance/insurance	social insurance	citizen guarantee and insurance
Administration	mix local-central state and market	corporative self-governance	state
Role of market	major	limited	minor
Role of means-test	major	limited	minor
Commitment to services	limited	limited	major
Commitment to full employment	minor	limited	major
Re-distribution	low	medium	high
Poverty	high	moderate	low

In focusing on differences, there is a danger in overlooking important commonalities and convergent trends. The Swedish model began in the 1960s to move in the German direction in the sense that a second-tier earnings-related insurance component was built on top of the older flat-rate universal system. The German model, in turn, has tentatively inserted a basic income guarantee, partly by upgrading the general social assistance scheme, and partly by introducing minimum provisions in pensions and unemployment, thereby approaching the Scandinavian model. The American model began with the Social Security Act of 1935 to move in the German direction of compulsory insurance; later, in the 1960s and 1970s, it moved marginally towards the Scandinavian notion of a citizen's guarantee with medical assistance for the aged and poor, and with supplementary pension assistance.

As welfare states have evolved and matured, they have therefore incorporated elements from one another. When need/work is emphasized as the basis of rights in the United States, that does not mean that the other models do not apply a needs principle; only that 'needs' figure prominently in the United States while only marginally in the two other cases. Regardless, it seems clear that the question is not just of variations of welfare around a similar basic standard, but of three distinct 'regimes'. This also emerges in the statistical overview in the next section.

III. Costs and effects: a statistical overview

This section undertakes a statistical comparison of the three welfare states in terms of their costs and effects. A welfare state may be effective in reducing poverty, but the costs involved are obviously an important consideration.

1. Social security costs

Aggregate social expenditure is a useful summary measure of a government's commitment to social security. Where governments insist on providing adequate protection to all, public social expenditures will inevitably rise. Table 2.2 shows, for the three countries, total government expenditure as a percentage of GDP on the cash and in-kind transfer programmes that are considered in this paper: medical care, sickness, invalidity, employment injury, unemployment, old-age and survivors, family, and maternity benefits, and public assistance (this is the ILO definition of social security expenditure). The data for 1983 are the most recent available on a comparable basis.

The differences in expenditure 'commitment' across the three countries are enormous. In 1983, Sweden spent one-third of GDP on social security; this figure was nearly two-and-a-half times that of the United States, with West Germany coming roughly in between. There has been considerable, but unequal, growth in all countries. Expenditure as a per cent of GDP roughly trebled during 1960-83 in Sweden, doubled in the United States and rose by only half in West Germany. In all countries, the growth rate has tapered off (and even declined) during the 1980s.

The figures for 1960 illustrate an important point: the cost of the Swedish "people's home" welfare state model was hardly greater at that time than that of the U.S. residualist model, despite being much more comprehensive. This can be explained by a combination of circumstances operating in Sweden at the time. First, although universal in coverage, the Swedish benefit levels in 1960 were modest. Second, the demographic

structure was favourable (see Table 2.3); the share of aged persons was smaller and, hence, so was the expenditure burden on the two costliest programs, health and pensions. Third, pension costs were contained through a high retirement age of 67. The big increases in costs in the Swedish model occurred when the second-tier earnings-related scheme was introduced, when the social services were expanded (these are especially costly in terms of manpower), and when an array of income/transfer-tested supplementary benefits were introduced.

TABLE 2.2 *Social security expenditure as a percentage of GDP*

	Percentage of GDP			
	1960	1970	1980	1983
Sweden	10.9	18.8	32.0	33.3
West Germany	15.4	17.0	23.8	24.3
United States	6.8	9.6	12.7	13.8

Source: ILO, *The Cost of Social Security*, Table 2, 1985 (figures for 1960-80), 1988 (1983). Social security expenditure taken to include medical care, sickness, invalidity, employment injury, unemployment, old-age and survivors, family, and maternity benefits, and public assistance.

A detailed analysis of the changing expenditure levels cannot be undertaken. However, some comment on what drives social security expenditures is appropriate. In all countries, a major part is allocated to pensions and health. Pensions go to the elderly by definition, so does a disproportionate amount of health expenditure: in 1980, some 52 per cent of public health expenditure in Sweden, 47 per cent in the United States and 33 per cent in West Germany went to the population over age 65 (OECD, 1988, p. 65).

Changes in pension and health expenditure are determined by demographic variation, and by policy choices regarding benefit levels and coverage. Table 2.3 shows how the proportion of the population aged 65+ has risen between 1950 and 1980. Demographic projections show that this will continue; it is estimated that by 2015 those aged 65 and over will represent over 20 per cent of the population of Sweden and Germany. This will represent a great burden on social security expenditure in the future.

The central and eastern European countries are also experiencing ageing populations, although the proportion of the elderly is, and will continue to be, less than in western Europe. Projections for 2025 put the proportion aged 65+ at 16.6 per cent in eastern Europe (excluding the USSR, where the figure will be lower) compared to 19.1 per cent in the

European Community (ILO, 1989a, Table A2). In fact, the figures for Sweden and West Germany for 2015 are higher than for any other European country, East or West (with the exception of Switzerland) (ILO, 1989a, Figure 1). Moreover, the eastern European economies' high female labour force participation rates (as in Scandinavia) are an important asset that will help finance higher expenditure on the elderly. This is crucial for the funding of PAYGO social insurance pensions. Hence, eastern Europe's relatively smaller elderly population and higher female participation rates may help alleviate the 'demographic crisis' that will occur in social security funding. The crisis can also be contained by raising the age of retirement, as is currently being done in some OECD nations.

TABLE 2.3 *The size of the elderly population*

% of Population aged 65+	Germany	Sweden	U.S.A.
1950	9.3	10.2	8.1
1980	15.5	16.3	11.3
2020 (projection)	21.7	20.8	16.2

Source: OECD, *Reforming Public Pensions*, 1988, Table 3.1.

Table 2.4 shows the past impact of demographic change on pension and health expenditure. Demographic change had little impact on health expenditure growth during 1960-81, but was important for pension expenditures. Still, it is clear from the table that policy changes have had just as much, if not more, impact. In the case of Sweden, policy changes in terms of increased benefits and coverage accounted for three-quarters of pension expenditure growth. In West Germany, the policy of encouraging early retirement — an increase in coverage — was responsible for the major part of pension expenditure growth during 1975-81.

Up to this point only *public* sector social security provision has been considered. Table 2.5 shows total (public and private) pensions and health expenditure, and the proportion of which is private. Note that the pension figures include means-tested transfers to the elderly. These are particularly important in the United States; had our attention been restricted to only the contributory OASDI pensions, this figure would have been lower.

On the face of it, there seems to be significantly lower pension expenditure in the United States. However, this is largely due to the difference in demographic structure in the three countries: the proportion of the population aged 65 or more in the United States is notably lower

TABLE 2.4 *The share of pension and health expenditure growth accounted for by demographic change*

	Percentage share of pension and health expenditure accounted for by demographic change		
	Germany	Sweden	U.S.A.
1960-75			
Pensions	49.2	26.4	29.2
Health	15.2	5.3	11.7
1975-1981			
Pensions	42.9	24.6	56.8
Health	0.0	8.8	26.3

Source: OECD, *Social Expenditure, 1960-1990*, 1985.

than in the other two countries (Table 2.3). When we adjust for this, the total pension expenditures in the three countries as a percentage of GDP are broadly similar to those on health; in this sense, costs do not vary much whether welfare is organized privately or publicly.

The pattern across countries regarding the importance of private provision is the same for both types of expenditure. In Sweden, where the welfare state is most generous, private sector provision is smallest; in the United States, where the welfare state is least generous, the highest private provision is found. The importance of private pension and health expenditure is similar in Sweden (less than 10% of the total), but in Germany and the United States, the private sector share of health expenditure is much higher than that of pensions. In fact, 80 per cent of U.S. pension expenditure remains public, while the public sector share of health expenditure is less than half, reflecting the lack of any comprehensive public health coverage.

The figures in Table 2.5 do not take into account tax expenditures which represent public sector expenditure, often in the form of a subsidy to the private sector. Information on these at a sufficient level of disaggregation is only available for the United States. In 1981, tax expenditures on employer and self-employed pension plans amounted to $38 billion, or 1.3 per cent of GDP (OECD, 1984, p. 82)[21]. Furthermore, the favourable tax treatment of social insurance pensions (OASDI for the retired) amounted to a tax expenditure subsidy of $11 billion to public pensions, or nearly 0.4 per cent of GDP. Taken together, these two tax expenditures alone represent about 20 per cent of the 1980 figure for total pension benefit expenditure in the United States, which is a substantial addition. It is worth noting that three-quarters of the tax expenditure is on private sector pensions. In 1981, tax expenditure on employer contributions to medical insurance premiums and medical care amounted to

$19 billion, or 0.65 per cent of GDP. This may be compared with figures for cash expenditure in the last line of Table 2.5.

TABLE 2.5 *Public and private pension and health expenditure as a percentage of GDP, 1980*

	Total expenditure as % of GDP	Proportion which is private
	PENSIONS	
Sweden	11.6	0.06
Germany	13.4	0.10
United States	8.6	0.20
	HEALTH	
Sweden	9.5	0.07
Germany	8.5	0.24
United States	9.5	0.57

Source: (i) Pensions: Esping-Andersen (1990, p. 84); public pensions include expenditure on means-tested benefits for the old, on disability, and on government service pensions; private pensions include both occupational pensions and private contract insurance plans. (ii) Health: OECD, *Measuring Health Care, 1950-1983*, 1985.

Table 2.6 shows expenditure (as a percentage of GDP) on active manpower policies in the three countries in 1987 (a year for which the OECD has compiled comparative data). Public sector expenditure on 'active' measures (employment exchanges, job placement services, training, employment creation, and mobility measures) is shown in the first column. The second column gives expenditure on 'passive' measures: unemployment compensation.

Sweden leads the OECD in terms of resources devoted to active manpower measures. (One of the main items in the Swedish labour market budget are measures to help the disabled, this accounting for 40% of the active expenditure — source as for Table 2.6). Active expenditure in the United States is markedly low, as it is also on passive measures. Although the American unemployment rate in 1987 was over three times that in Sweden (shown in the last column of Table 2.6), the United States spent less on unemployment benefits. The limited duration and (partly as a consequence) low coverage of the unemployment insurance system in the United States has already been noted.

One problem with the data on active labour market expenditures is that they are not sufficiently standardised to cover the *potential* problem which they aim to resolve. Although it seems unlikely, expenditure in Sweden could be particularly high because the Swedish labour market is characterised by severe problems. A clear measure of policy commitment

TABLE 2.6 *Expenditure on active labour market programmes and unemployment compensation as a percentage of GDP, 1987*

	Expenditure as percentage of GDP			
	Active measures	Unemployment benefits	Total	Unemployment rate, 1987 (%)
Sweden	1.86	0.70	2.56	1.9
Germany	0.99	1.33	2.32	6.5
U.S.A.	0.24	0.59	0.83	6.1
OECD 23-nation Average	0.72	1.22	1.94	—

Source: OECD, *Employment Outlook*, 1988, Tables 1.6 and 3.1.
Notes: Active measures include expenditure on employment services and administration, training, special youth measures, job creation and employment studies, and labour market measures for the disabled. The unemployment rate is the OECD standardised measure.

per relevant person is needed to supplement the picture given in Table 2.6. Table 2.7 provides such a measure, showing expenditure per participant in training courses as a percentage of GDP in 1988. Sweden spends over six times more per participant than the United States, with West Germany, as usual, coming in between. This further underlines the enormous gulf that exists between the active labour market expenditure of Sweden and the United States.

TABLE 2.7 *Expenditure per participant on labour market training for the unemployed and adults at risk of unemployment as a per cent of GDP per capita, 1988*

	Expenditure per participant as a percentage of GDP per capita
Sweden	60
West Germany	37
U.S.A.	9

Source: Scherer (1990, Table 5).

It is difficult to assess the pay-off of active manpower policies. If measured in terms of open unemployment, the high level of Swedish expenditure is unquestionably successful. Open unemployment has been kept below 3 per cent for many years. There is also no doubt that it is efficient in preventing long-term unemployment; only 8 per cent of the Swedish unemployed in 1988 had been unemployed for more than one year, compared to a European Community average of 50 per cent (OECD, 1989, p. 217; Commission of the European Communities, 1989, p. 117), although there may be other factors affecting the proportion of the long-term unemployed. Much less is known about whether training programmes, for example, succeed in matching people to appropriate jobs or in raising lifetime earnings [24].

2. The welfare state impact on poverty

Turning now to the effects of the welfare state, it is important to look at the extent of poverty in the countries concerned. The reduction of poverty is not, of course, the only goal of the welfare state; the alleviation of poverty is not the only criterion by which the expenditures we have just reviewed should be judged.

International comparisons of poverty are notoriously difficult. One of the principal problems is finding comparable data on incomes on which to base an analysis. This is one reason why the recent development of the Luxembourg Income Study (LIS) is so welcome; this project has collected comparable household data sets from many different countries, including the three examined here [25]. Tables 2.8 - 2.10 draw on analyses made on the LIS data by Smeeding, *et al.*, (1988) [26].

Table 2.8 shows the proportion of persons living in families in poverty *after* having taken social security transfers (and taxes) into account. The poverty concept used here is that of absolute poverty. The poverty line is defined as the value of a fixed basket of goods and services (adjusted for family size) deemed necessary for a minimum standard of living; the poor, on this basis, are those in families with income below this level. In Tables 2.8-2.10, we have used the official absolute poverty line of the United States which, for Sweden and West Germany, has been converted into national currency values on the basis of purchasing power parity exchange rates [27].

Table 2.8 *The extent of absolute poverty (Percentage of people in poor families)*

	Children	Adults	Elderly	Overall
Sweden (1981)	5.1	6.7	2.1	5.6
West Germany (1981)	8.2	6.5	15.4	8.3
United States (1979)	17.1	10.1	16.1	12.7

Source: Smeeding, *et al.*, (1988, Table 5.2).
Note: Families are defined as poor if their disposable income (adjusted by the U.S. poverty line equivalence scale) falls below the official U.S. three-person poverty line converted to other currencies using OECD purchasing power parity exchange rates. The data from the three countries refer to the following years: Sweden (1982), West Germany (1981), U.S. (1979).

Table 2.8 shows that 1 in 8 people are in poverty in the United States, compared to 1 in 12 in West Germany, and only 1 in 18 in Sweden. How sensitive are the figures to the definition of poverty? If a relative concept of poverty is used and if the relative poverty line is defined as 50 per cent of the national median income (this overcomes any

objection of imposing the U.S. poverty line of the other countries), the incidence of poverty rises in the United States to over 22 per cent, falls in West Germany to 5-6 per cent, and is unchanged in Sweden (source as for Table 2.8).

Not only are there differences between the countries in the overall level of poverty, but the relative position of children and the poor differs too. In Sweden, absolute poverty among the elderly is rare (it is virtually non-existent on the relative definition). In West Germany, poverty among the elderly is almost double that of other groups, and the elderly also fare badly in the United States. In other words, there are large differences in poverty despite the three nations' similar levels of total pension expenditure.

The United States really stands out for its high level of child poverty: more than 1 in 6 children live in poor families. The most recent data (referring to 1987) shows that this figure has risen to exactly 1 in 5 (Department of Health and Human Resources, 1989a, Table 3.E2). In the United States, both children *and* the elderly have a high risk of poverty in comparison with working-age adults.

To what extent is the considerably higher U.S. poverty rate attributable to its smaller welfare state? And, to what degree are the positions of the elderly and children in the different countries attributable to particular social programmes? Table 2.9 sheds light on the first of these questions. It shows the percentage of poor families (not individuals) using the same definition of absolute poverty, as in Table 2.8, (i) before taxes and public sector welfare state transfers (column 1), (ii) after taxes but before transfers (column 2), and (iii) after transfers as well as taxes (column 3) [28]. The final column shows the percentage of families that are poor on the basis of pre-tax and pre-transfer income, who are removed from poverty by the operation of the tax and transfer system.

The Swedish welfare state clearly wins in terms of the proportion of poor families that are brought above the poverty line. This is true for all three family types. In all three countries, very large numbers of the elderly are poor on a pre-tax/pre-transfer income basis (which is not surprising since they are less active in the labour market). The ability of the Swedish model almost to eradicate poverty among the elderly is confirmed — a clear result of the universal "people's pension" system. Even the U.S. system manages to bring two-thirds of the aged above the poverty line.

The differences in success in removing families with children from poverty are, however, notable. Only 1 poor family with children in 6 are removed from pre-tax/pre-transfer poverty by the U.S. tax and transfer system, and slightly less than 1 single parent family in 8. This compares with over a half and three-quarters, respectively, in Sweden. The U.S. welfare state system fails, quite abysmally, to reduce child poverty sub-

stantially. The German system is, for once, hardly better than the American, slightly worse for families with children and about the same for single parents. However, the much lower level of pre-tax/pre-transfer poverty among West German families with children should be taken into account: one would expect it to be harder to achieve large percentage reductions when the amount to be reduced is small [29].

TABLE 2.9 *Poverty reduction and the effect of taxes and transfers*

	1.	2.	3.	4.
	Per cent of families which are poor			
	Pre-tax Pre-transfer	Post-tax Pre-transfer	Post-tax Post-transfer	Poverty reduction rate (%)
Families with children				
Sweden	10.4	22.5	4.4	57.7
West Germany	7.9	15.0	6.9	12.7
United States	16.6	18.0	13.8	16.9
Single-parent families				
Sweden	33.1	49.4	7.5	77.3
West Germany	37.2	47.1	31.9	14.2
United States	49.3	51.4	42.9	13.0
Elderly families				
Sweden	87.9	98.1	2.6	97.0
West Germany	80.6	82.2	17.1	78.8
United States	59.0	59.8	18.7	68.3

Source: Smeeding, *et al.*, (1988, Table 5.12).
Notes: i) Poverty defined on an absolute basis — see notes to Table 8. ii) The poverty reduction rate in column 4 is defined as column 1 minus column 3 divided by column 1 (×100). The data from the three countries refer to the following years: Sweden (1982), West Germany (1981), U.S.A. (1979).

A focus on the overall poverty reduction of tax and transfer systems disguises the separate effects of the taxes, on the one hand, and the transfers on the other. The figures in the second column of Table 2.9 are important, since they show the intermediate effect of the tax system alone, although these figures do need to be treated with some caution. If transfers are subject to tax, then it is much harder to disentangle the tax and transfer system than the analysis in Table 2.9 suggests [30].

This study restricts itself to families with children. The figures bring out the relatively generous tax treatment of lower income families with children (one- or two-parent) in the United States. The tax expenditures

targeted at children, especially lower down the income distribution, result in the tax system producing only a small increase in child poverty[31]. Compare this with the situation in Sweden and Germany where post-tax/pre-transfer poverty is double that of pre-taxes. This is because higher government expenditures result in a higher tax burden. In other words, the U.S. system takes little away in taxes, but gives little back in transfers; in Germany and Sweden there is more taking and even more giving back (especially in Sweden). This means that there is considerable 'churning' in the Swedish and German welfare state (the state giving with one hand and taking it away with another) to which some may object, but the result in terms of poverty alleviation is apparent.

How poor are the poor who remain below the poverty line after taxes and transfers have been taken into account? Table 2.10 shows the average percentage shortfall from the poverty line for families who continue to be poor: the average 'poverty gap'. Again, the United States stands out as the country which leaves the poor the least well-off. On average, poor families with children in the United States have incomes which are still 38 per cent short of the poverty line after the receipt of all transfers and deduction of taxes, compared to 24 per cent in West Germany and 29 per cent in Sweden.

TABLE 2.10 *Average poverty gap of families remaining poor after taxes and transfers*

	Average percentage shortfall from the poverty line	
	Families with children	Elderly families
Sweden	28.4	3.0
West Germany	24.1	26.5
United States	37.7	29.3

Source: Smeeding, *et al.*, (1988, Table 5.1).
Notes: For the definition of poverty, see notes to Table 8. The data from the three countries refer to the following years: Sweden (1982), West Germany (1981), U.S.A. (1979).

Is it possible to explain Germany's and (especially) Sweden's superior capacity to reduce child poverty by their universal child allowance schemes, something that is notably lacking in the United States? This is a difficult question to answer. Suppose that a poor family receives both a social insurance benefit and family allowance, pushing it above the poverty line. It may be the combined effect of the benefits which has done the job, or it may be that either transfer was sufficient to remove them from poverty. In

neither case can one ascribe the poverty alleviation to a particular programme. Similar problems apply to any analysis of transfer-induced reduction of the poverty gap [32]. Moreover, in the same way as benefits may be subject to tax, different transfers may not be independent. For example, child allowances may be taken into account in the calculation of means-tested benefits. A full analysis of the impact of particular transfer programmes would need to look at each transfer under the assumption that the others do not exist. This requires a tax-benefit simulation model (of the type described in Atkinson and Sutherland, 1988).

Summary

The extent of poverty varies considerably between the three countries, reflecting in part their different welfare state expenditure commitments which in 1983 varied from 14 per cent in the United States to 33 per cent in Sweden. Poverty is notably higher in the United States, where the least is spent on the welfare state. The extensive use of means-testing in the United States, which some might argue should effectively target resources to those in need, is not associated with lower poverty rates, although this may also be due to the holes in the U.S. means-tested system. Child poverty in the period covered by the LIS data, 1979-82, varied from 5 per cent in Sweden to 17 per cent in the United States and official analyses indicate that the U.S. child poverty rate has risen more recently. Since the large American private welfare system caters mainly to those already well-off, its effect on poverty reduction is likely to be marginal. In the case of the elderly, American poverty rates were very high even if total private and public pension expenditures were similar to those in Germany and Sweden.

Finally, it should be repeated that this analysis has considered only the effect of the welfare state on poverty; the wider issue of inequality or its effect on economic productivity and incentives to work has not been looked at. Neither have the details of welfare-state financing in terms of the different tax and social insurance contribution rates faced by individuals and firms been considered.

V. Conclusions

This chapter does not attempt to draw lessons that are directly applicable to central and eastern Europe, since this would involve detailed discussion of the present situation in the region. Nevertheless, some general observations relevant for central and eastern European policy makers can be made.

First, there is no such thing as a typical OECD welfare state. This study has identified three very different models involving quite different

combinations of universality, social insurance, means-testing, private provision, tax expenditures and labour market policy. Hence, central and eastern European governments do have a choice; the introduction of the market system does not imply that welfare state provision need take a particular form.

Second, none of the three welfare state models considered relies on private markets to provide the bulk of social protection. The existence of market failure is one important reason for this. Health care in the United States is the only case where private sector cash expenditure is greater than that of the public sector but, again, we should recall the degree to which private sector health plans are subsidized by tax expenditures. A heavy reliance on the private sector would put central and eastern European countries out of line with practice in the OECD area.

Third, it is apparent that the choice between welfare state models has implications for overall public expenditure burdens, on the one hand, and on poverty and distribution on the other hand. This is most clearly evident in the contrast between Sweden (high costs/low poverty) and the United States (low costs/high poverty). Such contrast, however, is far less stark when total (i.e., public and private) expenditure and demographic structure is taken into consideration. The implications for central and eastern European countries are less clear here, however, since this analysis of cost and impact refers to countries with a much higher standard of living (in terms of GDP per capita). The welfare states of OECD countries 30 years ago may be worthy of further analysis, although, as mentioned in the Introduction, there are serious problems of comparison.

No welfare state model is perfect. Each has its strengths and weaknesses, advantages and disadvantages. The main advantages of the German social insurance type model is that it strengthens the incentive to be in the labour force, and that it gives recipients the idea of a contractually inviolable right to benefits; it also offers benefits that are well-tailored to accustomed living standards and thus assures the individual against sudden income-shocks during the life-cycle. The weaknesses of the social insurance model are clear: it leaves out sometimes large groups whose labour market attachment is marginal, and does not function well for those having experienced career interruptions and an unstable working life. The social insurance model found in Germany requires long contribution records and lengthy maturation periods which means that it is not a well-suited option for dealing with immediate social problems. One solution to the latter problem is to 'blanket in' the ineligible groups from the beginning, as did the United States during the formative years of social security.

A social assistance model has the advantage that benefits are distributed on the basis of demonstrable need, and it thus solves one of the

principal problems of social insurance. But it has several well-known disadvantages. First, it requires a costly administrative apparatus to ascertain need, introduces a strong element of paternalism and control that brings in its train a pervasive sense of social stigma; hence, it may not reach many groups in real need due to problems of low take-up. Its target-efficiency may, therefore, be far less than optimal.

A system relying heavily on private social protection has certain advantages. It would appear attractive in cases where the government has difficulty raising tax revenue (or does not wish to do so). It is also said to give greater freedom in choosing a welfare package that suits the individual (assuming ability to pay). Its weaknesses are evident. Private plans almost inevitably fail to reach those who need protection the most (market failure), and they are almost by definition likely to be distributionally less egalitarian. Where private plans are attached to companies (as is often the case), they risk producing severe rigidities in the labour market. It is probably also safe to say that private programmes have difficulty growing without public subsidies (e.g., through tax-concessions), making their private market status somewhat dubious.

The universal "people's home" model, as it was developed in Scandinavia after World War II, is, in many respects, an attractive option. If stripped of later refinements, in particular its expensive second-tier earnings-related pension, it offers a basic safety net at a relatively modest cost for the entire population across all the main social risks. One of its great achievements was to construct a strong sense of basic equality and solidarity of citizenship, a factor of considerable importance for the legitimacy of taxation and the 'welfare state' more generally. Since benefits are distributed automatically to all, it is also administratively simple and economical. It has been criticized for the apparent waste that goes with giving benefits to all, including those who do not need them. This criticism, however, is less valid if, in return, governments tax the value of the benefits given to the rich. The greatest weakness of the "people's home" model is that it does not satisfy the needs of more well-to-do groups as benefits are comparatively modest. The basic universal model will thus generate pressures for either market supplements or for an upgrading of public programmes among higher income groups. This leads to substantial cost escalation, as has been noted.

With these pros and cons in mind, it is evident that simple cost-effective accounting will not suffice in deciding on the relative merits of one or another model. The choice between social policy alternatives depends in the final analysis on the conditions in each country: the composition of its labour force, its demographic profile, its level of economic development, its culture, and its political will.

NOTES

[1] For example, social insurance expenditure represented 15.5 per cent of GDP in Hungary in 1988 (National Administration of Social Insurance, 1989, Table 2.4).

[2] In 1950, average GDP per capita in the three OECD countries we consider in detail in this paper was $3,207 in 1975 prices. This compares with average 1980 GDP per capita (again in 1975 prices) of $3,379 in Hungary, Poland and Romania (Summers and Heston, 1984). (GDP valued using purchasing power parity exchange rates; averages not weighted by population size.)

[3] In the United Kingdom in 1985/86, administration costs of the means-tested programme Supplementary Benefit (a social assistance benefit for which any person not in full-time work may apply) represented 11.3 per cent of total expenditure, compared to 1.9 per cent for the universal family allowance Child Benefit, and 3.5 per cent for the National Insurance scheme (HMSO, 1989, Table 15.23 and Department of Social Security, 1988, Table 44.04).

[4] Although we should note that market economies do not, of course, offer unconstrained choice to all unconcerned. Existing regulations in the labour market are described in Emerson (1988).

[5] Before World War II, trade-union type friendly societies constituted a fourth important group, but their role has by and large disappeared (trade unions maintain an administrative role in unemployment insurance schemes in Scandinavian countries). It is sometimes difficult to define what is private and public social protection. Civil servants' benefits are distributed by the government, but are typically equivalent to occupational benefits. Vice versa, it is often the case that private organizations administer what are, de facto, public social programs. In Germany, for example, private associations (typically non-profit) are widespread in health care delivery, but they function within a framework of government-defined standards.

[6] Social insurance is typically made compulsory so as to prevent average premiums rising which would occur if low risk individuals could opt-out.

[7] Although the failure of governments to fully index pensions in social insurance schemes shows that public provision does not necessarily lead to better protection.

[8] If the odd house burns down, there is no pay-out problem for a fire insurance company. But if a whole city goes up in smoke, then a potential bankruptcy problem may exist.

[9] There are other inefficiency arguments that can be made against private provision. For example, an unregulated occupational pension industry may reduce labour market mobility if workers are unable to take pension rights with them when they leave the firm.

[10] It is said that the average American hospital must employ more than 30 billing clerks.

[11] This point is developed in the context of unemployment compensation in Atkinson and Micklewright (1990).

[12] Descriptions of details for the three countries can be found in Gordon (1988), Department of Health and Human Resources (1989) and Hagen (1990).

[13] The pension for an early retiree at age 62 would be, on average, 70 per cent of the standard pension.

[14] As far as the unemployed are concerned, from October 1990 all states must extend the possibility of AFDC to unemployed parents but eligibility may not be indefinite. Prior to this date AFDC could be received by unemployed parents in only about half the states but compared to UI, coverage was low. In August 1988, there were 194,000 families with an unemployed parent receiving AFDC compared to 2.5 million individuals in receipt of UI (*Social Security Bulletin*, January 1990, Tables M-30 and M-34).

[15] It has been estimated that in 1974, 20 per cent of the non-institutionalised would have qualified for SSI but only half of these applied (Warlick, 1982).

[16] Although Food Stamps are formally an in-kind benefit, there is some evidence that they may be traded by recipients and can thus act like a cash transfer (Moffit 1989).

[17] For a person paying the higher marginal rate of tax of 28 per cent, the allowance for each child was worth about 3 per cent of the average production worker earnings in 1988 (Atkinson and Hills, 1989). For high incomes, the allowance would be progressively withdrawn.

[18] Flat-rate pensions are financed by an ear-marked tax but the payment of the tax is not a pre-condition for pension receipt. The details of the national health system is described by Gordon (1988, pp. 209-10).

[19] The figures for the United States apply to Pennsylvania which, in 1979, came about half-way in the rankings of AFDC generosity.

[20] The minimum annual income that qualifies an individual under the scheme is only about one third the average worker's income. This means that even most part-time and extremely low-paid workers are insured — a factor that helps diminish pension differentials between men and women.

[21] The duration of sickness benefit can be extended up to 260 weeks.

[22] By transfer-tested benefits we mean benefit supplements that are automatically granted to persons when the level of normal benefits are inadequate. They should be clearly distinguished from income-tested benefits in the sense that eligibility depends primarily on an assessment of the adequacy of social benefits.

[23] In calculating the percentage of GDP in 1981, a figure for the latter of $2,923.8 billion was used (OECD, 1985, p. 85).

[24] Holmlund (1990) reviews the evidence for Sweden.

[25] It is worth noting that data from several eastern European countries are being deposited in the LIS and will allow the pre- reform situation in those countries to be widely studied and compared, both with each other and with OECD countries.

[26] See also Smeeding, *et al.*, (1990).

[27] The official U.S. poverty line, in fact, takes the price of a basket of food only (chosen to represent a minimum adequate U.S. diet) and multiplies this by the reciprocal of the average food expenditure to net income ratio (there are adjustments for family size).

[28] The figures in Table 8 differ from those in column 3 of Table 9 because the former relate to individuals and the latter to families.

[29] The figures for Germany also appear to be sensitive to the definition of the poverty line. When a relative concept is used, the LIS data suggest that West German system performs well in removing people from poverty (Smeeding, *et al.*, 1990, Table 3.5). The conclusions for the United States and Sweden are unchanged.

[30] Merely subtracting transfers from ex-post incomes will not be sufficient to arrive at the post-tax/pre-transfer position because the impact of the tax system on transfer receipt will remain in the data.

[31] The effect of the tax system on poverty in the United States may be even less in 1990 than in 1979 when the LIS data were collected. Atkinson and Hills (1989) note that the 1986 Tax Reform Act re-instated the principle that those below the official poverty line should not be paying tax and by raising allowances nearly 5 million people were removed from tax.

[32] On the basis of their analysis of the LIS data, Smeeding, *et al.*, argue that "social insurance is overwhelmingly more important" (1988, p. 112) than child-related benefits in reducing the poverty gap. This conclusion needs to be treated with extreme caution. The statement, and the table on which it draws, applies not to reduction in the poverty gap itself but to the total of public transfers to the poor defined on a pre-tax/pre-transfer basis

divided by the poverty gap. This figure is not bounded by an upper limit of one since transfers may push some formerly poor people well above the poverty line (in the case of Sweden, the ratio just described takes the value 1.76 for families with children). It may be that child allowances alone are sufficient to close the poverty gap for some people and that social insurance then takes people further away from poverty line. The focus by Smeeding, *et al.*, on the total of public transfers to each family will mask this.

CHAPTER 3

SOCIAL SECURITY SYSTEMS IN THE NEW DEMOCRACIES OF CENTRAL AND EASTERN EUROPE: PAST LEGACIES AND POSSIBLE FUTURES

Zsuzsa Ferge

I. The existing social security system

1. AN EAST-WEST OVERVIEW

On the face of it, the social security system of the state socialist countries in Europe did not differ fundamentally from that of the developed market economy in general. If one studies international handbooks, such as *Social Security Programs Throughout the World* published by the United States Department of Health and Social Services, or *The Cost of Social Security* published by the International Labour Office, the great dividing line has never been between 'socialism' and 'capitalism', but rather between both of them, and the Third World, or Europe together with North America, Japan, New Zealand and Australia, on the one hand, and the remaining continents, on the other. By 1980, the cost of social security in terms of the GDP was well over 10 and often over 20 per cent in the huge majority of the countries in the first group (with the exception of Turkey). In the second group, which accounts for well over 100 countries, the ratios were much lower: those countries in which the cost of social security attained 10 per cent of GDP were the exception (i.e., Chile, Israel and a few others — see Table 3.1). The same pattern emerges if one looks at the number of social security programmes in the two groups of countries (see *Social Security Programs Throughout the World*, 1985). In short, there was apparently nothing wrong with the commitment to social security by state socialism.

Among the countries with a developed social security system, there were few conspicuous differences between market capitalist and state socialist countries. As for the positive deviations of socialism (again, based only on formal, legal or statistical criteria), it seems that state socialist countries had slightly more generous programmes for children and

TABLE 3.1 *Expenditure on social security benefits (Percentage of GDP or NMP)*

Economy	1960	1965	1970	1975	1977
Developed market	9.3	10.4	11.9	15.6	16.6
Centrally planned	—	11.7	12.8	14.4	14.9
Developing *					
Africa	—	—	3.5	3.5	3.8
Asia	—	—	2.8	2.4	2.7
Latin America	—	—	3.9	3.8	4.2
'Exceptions':					
Chile	—	9.8	15.6	8.5	9.4
Israel	5.8	5.2	7.2	9.4	12.0
Turkey	1.3	1.6	3.0	2.9	3.3

Sources: *The Cost of Social Security* (1981), Geneva: ILO; *Report on the Social World Situation* (1982), New York: United Nations.

TABLE 3.2 *The average number of social security programmes by type of country * 1987*

Developed market economies (24 countries)	5.00
Centrally-planned economies (9 countries) [a]	4.44
Developing countries (107 countries)	2.71

Source: Author's calculations based on *Social Security Programs Throughout the World - 1988*, Washington: United States Department of Health and Social Services.
* The five programmes which make up the maximum average consist of: old age, sickness, occupational injury, unemployment, family allowance.
[a] China and Cuba are also included in this group.

mothers (in terms of family allowances or maternity leave, for example) [2] than the other countries, except perhaps in Scandinavia (Gacs, 1990). On the negative side, state socialist countries were conspicuous for the simultaneous absence of three elements: unemployment benefit programmes, [3] universal programmes in general (the single exception as late as 1987 was East Germany which had a universal family allowance system), and programs for automatic indexation even in case of pensions existing in several, if not all, capitalist countries.

A more general, statistically less controllable difference is the general framework of social security. In most western countries it has been recognized that classical, or Bismarckian, social insurance is just one element of the welfare system and that the genuine protection of existential security can be attained only by a social security system. In some cases the two approaches have been integrated, at least partly. In other cases, social insurance and social assistance provisions continued to co-exist. In socialist countries, only social insurance, namely, employment-related

benefits, have become accepted. Social security, as a more fundamental concern, has been ignored, even if some forms of social assistance have occasionally survived, as in Poland, or have sneaked back, as in Hungary.

This peculiarity is partly due to the fact that the economy was supposed to work in a way which would solve all social problems, including existential security. The instruments were (artificial) full employment; social insurance covering all employees (and it was assumed that everybody sooner or later would become a state employee); pressure on state firms to build up welfare provisions (such as company kindergartens, holiday homes and, especially in the Soviet Union, even hospitals); a wage system with relatively limited differentials so as to ensure living wages for all; and a heavily subsidized, non-economic price system. In fact, the essential items of consumption — rent, fuel, basic food, public transport, most services (hairdressing and public laundries included) have operated with grossly subsidized prices. These prices operated as a sort of universal benefit. They assured access to basic needs even with a very low GDP in the early sixties and with a low wage level. Over the last few years, with increasing incomes and a changing structure of subsidies, the social distribution of many (if not all) subsidies has become rather lopsided, favouring the better-off groups (Abel, 1990). Therefore they should be questioned not only on efficiency, but also on equity grounds. The other side of the coin was that the subsidized price system was a lasting pretext for maintaining wages at a low level. It could be argued that centrally set wages could not have covered 'unsubsidized' needs. According to all economic analyses, this solution was detrimental to the economy, and in fact it did not solve many social problems. For instance, it subsidized those having already a home, but had no provision for access to a first flat.

It still remains to be seen whether this instrument was altogether dysfunctional or whether the practice can be justified under certain historical conditions. In most state socialist regimes, the 'social economy' helped to overcome massive pre-war poverty and established basic existential security by means of full employment and social insurance. The recent collapse of the 'socialist' system and the rapid return of the secular problems of poverty, insecurity, or unemployment tend to prove that even these genuine achievements were based on quicksand — on a sick economy and on dictatorial, illegitimate politics.

The rejection of the concept of social security, in a broad, sense and the proposed remedy of establishing an organic relationship between social policy and the economy — with all its functions and dysfunctions — was a distinctive feature of state socialism.

2. A SEARCH FOR THE EXPLANATION OF EAST-WEST DIFFERENCES

i) The ideologically-based system

There are many ways of grouping and analyzing social security systems (see Chapter 2). The classification which follows is only an *ad hoc*, heuristic tool devised for the better understanding of state socialist social policies. A distinction may be between the following types:

a) Need-oriented systems, with politics genuinely committed to satisfy those needs of the citizens which are agreed upon via a democratic political process.

b) Pragmatically evolving systems, in which the political decision makers are intent on avoiding conflicts around social issues. The aim is not genuinely to satisfy needs, but to obtain quiescence. Hence, the solutions may be real or formal and stop-go methods (i.e., an alternation between yielding to claims and withdrawing commitments according to the fluctuation of political forces) may be used quite often.

c) Ideologically constructed systems, in which the needs to be satisfied by public resources are defined in conformity with the requirements of the ideology — as that ideology is understood by the decision makers. Hence, the use of public resources may or may not correspond to what people really want, and the solutions may be, and usually are, more formal than real. The objective is not genuinely to satisfy needs, but to have formal (statistical or similar) proof of the fulfillment of the ideological tenets.

The social policy and social security systems of most developed market economies belong probably to the second type, with pragmatically forged answers to oscillating political scenes. However, time and again some country may come really close to the first truly 'ideal system'. This may happen if social solidarity is at its high point and political decision makers are elected, and act, in conformity with this climate (as was the case possibly in Sweden in the thirties, in Britain at the end of World War II, or more recently in post-Franco Spain).

The socialist countries of central and eastern Europe obviously belonged to the third type. Their policies — economic, social, cultural, or other — were shaped by the dominant ideology, crushing everything and everybody by the manner of its application. While the balance of this historical experiment is altogether so negative as to justify the collapse of the system, it would be too simplistic to condemn in a wholesale way everything which happened during the past decades. In fact, unlike fascist ideology, the socialist ideology had many elements attractive to those in favour of a more just and more humane society. In a sense, social policy constituted probably the only field where the ideological approach to

reality has had considerable beneficial consequences. In most other spheres of life — politics, economy, culture, law, religion — the central power imposed models on reality which were artificially invented, which had no grass roots, which were forced upon society from the top and which, therefore, were never made legitimate by the popular will. The main exception in the economy was the land reform of 1945. The first act of the new, democratic post-war government was the distribution of the big, feudal estates among the landless peasants, who became thereby individual smallholders. This reform could claim its legitimacy through long-standing popular claims and bitter fights ever since 1848. Nevertheless, central planning, a parliament without parties, or local authorities without any autonomy were purely artificial constructs, without the support of any constituency.

In the case of social (and even more broadly in societal) policy, the situation was different. In all central and eastern European countries, there were, before World War II, trade union movements (sometimes very strong), social democratic parties which waged bitter fights for better wages or for full employment. In practically all of these countries, the social security system was established before the second World War, even if on a reduced scale (see Table 3.3). Free education and free health care were explicitly claimed. In some cases (especially in central European countries) there were vocal feminist groups struggling for the emancipation of women.

All in all, most social policy objectives incorporated in socialist ideology corresponded to already articulated popular claims and many of them already had local traditions. It was probably only in the case of social policy that 'socialist achievements' had an organic link with social reality, and that, at least for a while, they were considered by many as legitimate. However, even in these cases, the development of the systems was flawed essentially because of the supremacy of ideology and of the totalitarian nature of the power structure.

ii) The negative role of ideology

Ideology emphasized the primacy of so-called productive branches over any other activity. Hence, all the sub-systems outside the economy (social welfare in the first place) were considered of secondary importance and were handled residually by the budget.

The over-emphasis on paid work as the single most socially valuable activity influenced the evaluation of people. Current (paid) active workers had much more 'social value' than unpaid workers (mothers for instance), or would-be workers, the children. But even children fared better than those who, because of sickness or age, were never to return to the labour force.

TABLE 3.3 *Adoption of the first social security laws in European countries according to the situation in 1985* [1]

Period	Enactment of the first law on				
	Work injury	Sickness & maternity	Old age, invalidity, death	Unemployment	Family allowance
Between 1883 & 1900	11	7	2	—	—
Between 1901 & 1920	10	11	12	11	—
Between 1921 & 1944	4	8	11	7	11
After 1945	—	1	1	3	15
Total	25	27 [2]	26 [3]	21	26
Average year	1907	1914	1918	1925	1945
Enactment in central and eastern European countries					
Bulgaria	1924	1918	1924	1925	1942
Czechoslovakia	1887	1888	1906	—	1945
Hungary	1907	1891	1928	1957 [4]	1938
Poland	1884	1920	1927	—	1947
Romania	1912	1912	1912	—	1944
USSR	1912	1912	1922	—	1944
Yugoslavia	1922	1922	1922	1927	1949

Source: *Social Security Programs Throughout the World - 1985*, U.S. Department of Health and Human Services, 1986.

[1] 25 countries altogether, excluding Albania and Turkey, and also Malta and Cyprus (independent only after the second World War).

[2] In Italy and Spain, sickness and maternity insurance were enacted in two different years.

[3] In Denmark, there are two old age and two injury laws.

[4] This law was practically never implemented. It was revoked in 1986.

From this perspective, only distribution according to work was justified. This meant that the condition of obtaining social security benefits — including those for children — was paid employment. This ideological commitment went so far as to deny even social assistance to needy families with children if both parents did not have a job. This strict rule was relaxed only in the last years, but it still influences the discretionary decisions of local authorities. In fact, the biblical prescription that "those who do not work, should not eat" was rigidly applied.

Ideology emphasized the supremacy of the collective over the individual interest. The total absence of response to individual needs, or needs of particular groups, followed as a matter of course. This was another reason to abolish social assistance in the early years of state socialism. Some of its forms slowly crept back in most 'socialist' countries from the sixties on. But, because social assistance did not fit the new ideology, it was revived

in its 19th century form. To this day, social assistance, wherever it exists, has remained discretionary and stigmatizing and is handed only to "the deserving poor". This goes so far in Hungary, for instance, as to deny assistance to 'undeserving' children, too. According to the regulation of 1974, if a child is absent from school for at least two days without justifiable reason, the assistance has to be withdrawn from the family.

Social services, including social work, were also wiped out around 1950. They started to re-emerge only in the mid-seventies. But social work as a qualified profession was not recognized until recently, and the education and training of social workers is just starting up in some of the former socialist countries.

Ideological supremacy denied reality. Any facts which did not fit the ideology were ignored or denied by the central power. It was obvious, therefore, that there could be no provision for existing hardships. Examples abound: since the existence of poverty was denied, social assistance was naturally abolished. Since homelessness, unemployment or inflation were declared to be absent from socialism, there were no shelters for the homeless, there was no unemployment benefit, and the regular indexation of benefits was non-existent.

iii) The impact of totalitarianism on social policy

Because of the totalitarian nature of power and of the absence of democracy, every step which improved the welfare system was presented not as the response to popular claims, but as the benevolent gift of the party-state, which it both initiated and carried into effect. Therefore, the original legitimacy of social policy was slowly eroded by the lack of the citizens' participation in shaping the system.

All the systems were reorganized so as to ensure full central control and to exclude participation. The self-government of social insurance was abolished. The relative autonomy of the agents and actors (i.e., hospitals or doctors) was fundamentally curtailed. Moreover, welfare policy was, in many cases, used to destroy local bonds or other ties (Ferge, 1988).

Because of the over-centralized and undemocratic nature of power, the ideological commitment to equality did not ensure equal access to, or equal treatment in, many institutions. Regional inequalities have remained enormous in terms of access to health care, and social inequalities (shaped by unequal power, unequal knowledge or unequal money) have permeated most institutions and relationships.

The residual character of social policy and the unresponsiveness of the central power led, in many instances, to shortages. Endless queuing bred various forms of corruption.

The concept of social rights was absent from the political vocabulary and ignored factually. All forms of social assistance remained discretionary, without any possibility of appeal. Even in case of litigation about social insurance benefits, there was no possibility of obtaining redress by an independent authority.

Moreover, the only concern of the top decision makers was that of proving their ideological commitment. They were not interested in real, only in formal achievements. They needed impressive statistics; not effective, efficient, and humane systems. Therefore, only formal and formally controllable elements were followed up, without a second thought for the quality of benefits or services.

The predominance of the formal over the real has been one of the major characteristics of state socialism. High growth rates in production, based on gross output figures, went hand in hand with deteriorating standards and even with diminishing outputs of goods fit for consumption. For example, the significant increases in school enrollment at all levels matched increasing functional illiteracy because the quality of teaching rapidly degenerated.

In social security, the formal, statistically registered increase in the number of beneficiaries, and of total expenditures, was accompanied by basic deficiencies both in the overall system (e.g., the absence of indexation) and in day-to-day contacts with beneficiaries (long waiting periods between retirement and the moment of getting the first pension, demeaning treatment of clients, oppressive practices in institutions and so forth).

Totalitarian politics have also been responsible for neglecting individual needs. In fact, there was no social or political movement which could have spelt out unfulfilled or new needs, and there were no pressure groups to support these demands. In all the cases not provided for by the overall system, people were alone to fend for themselves as best they could. That is why it is a basic error to qualify state socialism as a 'paternalist' system.

To sum up, one can admit that the totalitarian system did create some important welfare institutions (social insurance, public health) which were formally similar to those emerging in western welfare states. While such institutions, operating on a large scale, have been instrumental in reducing massive poverty and certain inequalities, their mode of operation followed the totalitarian logic: their importance was always secondary to the so-called productive sphere; they operated in an uncontrolled and undemocratic way; they have remained insensitive to most minorities and to individual needs; instead of becoming institutions of public service, they became agents of political domination.

As a consequence, it was not only politics and the economy which were distorted by state socialism. Welfare politics was no exception. The organic integration of social policy and the economy, together with the

totalitarian nature of power led to the perversion and ultimately to the crisis of all the sub-systems — welfare policies included. The radical change of the system became inevitable.

II. How the social security system is affected by the change of the economic and political system

1. Some new trends

The above analysis clearly points to the need for change, but also to the main difficulties of a transition to a market economy and parliamentary democracy.

The 'socialist' economy was constructed so as to eradicate fully the market logic. The reconstruction of the market is currently understood to mean the elimination of all those 'social' elements which were built into the economic system and which clearly have had a non-market, or anti-market character.

This implies, among other things, the withdrawal of the state and the replacement of direct state intervention with fiscal and monetarist measures. The consequences imply serious social problems.

One case in point is the fundamental change in employment policy. The closing, or bankruptcy, of inefficient firms leading to the elimination of all jobs, as well as all those deemed 'unnecessary' throughout the economy seem to be necessary conditions of market efficiency. The threat of unemployment has already appeared everywhere. In Poland, those registered as unemployed numbered 1,400,000, or 10 per cent of the labour force, in December 1990 [4]. In Hungary, in November 1990, there were 70,000 registered unemployed (*Nepszabadsag*, 9 January 1991) with three or four times as many unregistered [5], and with rather dismal perspectives. Czechoslovakia had 60,000 registered unemployed at the end of 1990 [6]. The unemployed (registered and unregistered together) are usually heavily concentrated in already poor or declining regions and among disadvantaged groups (gypsies, the unskilled, the young, women, the sick or the elderly). Among the registered unemployed, though, the share of skilled workers and white collar workers is growing.

The basic change in wage and price policies has also far-reaching consequences. According to market theory, state control over wages has to be given up, and state subsidies for goods and services have to be abolished. In practice, the state still controls wages and is instrumental in fixing prices. The direct corollary of the elimination of price subsidies, reduction of budget deficits and currency devaluation is a high inflation rate which is already present in some countries (Hungary, Poland or Yugoslavia) and is almost inevitably threatening the others. The net result

is a continuous decrease of real wages and of living standards for pensioners, families with children, and other beneficiaries due to only partial indexation of social benefits.

One important ingredient in the social policy of state socialist countries was that the state shifted many of its social responsibilities to the workplace. Thus the workplace performed an important social function by offering welfare services (from medical care to kindergartens). Those services are currently questioned in the name of economic rationality and market efficiency, and may be withdrawn before other arrangements are made.

All the above trends are in practice redistributing income and opportunities from the poorer to the better-off segments of the population. This may be an unintended consequence, but one which could be anticipated and which is supported by rather strong interests (Miller, 1987). The redistributive impact of inflation is well known. At the workplace, services and benefits which benefit the majority are being curtailed, while those favouring only the upper echelons are on the increase (with the introduction of private pension schemes, the multiplication of company cars and so forth). Absolute and relative poverty are on the increase and have become burning issues in most countries.

The above developments are underpinned by a rapidly spreading neo-liberal ideology. While neo-liberalism is on the rise everywhere, its attraction is probably even greater in former state socialist countries than elsewhere. This may be due to the utter failure of the planned economy, to the connection between market and political freedom (partly real, partly imagined), and also to the disorganized state of social forces. At present, those groups which presumably benefit from an unfettered market are much more vocal than those which may be losers.

The building up of democratic politics is no small task, either. The majority of new democracies (with the exception of Czechoslovakia) had no strong democratic tradition, and, over the last 40 years, whatever notions there were have been buried. The political scene is muddled, and paltry power struggles may take precedence over genuine politics. In social policy, the acceptance of citizens' participation in shaping the new welfare system and the democratization of institutions, which would be a difficult task anyway, has not yet been clearly put on the agenda. Decentralization, which is an important tool of democratization, is a particularly difficult process. The reconstruction of local government bodies would be a difficult process anyway. It is rendered doubly difficult by the rivalry of central and local agencies and by the historically ingrained propensity of the central state to retain as much power as possible. Hence, the local authorities may find themselves in a tight situation, with many new responsibilities, but without adequate resources and entitlements.

2. The challenges facing social policy

The above-mentioned changes imply formidable challenges to welfare politics. Social policy must now expect to deal with their consequences, but the difficulties are tremendous. Expertise and resources may be insufficient. Most importantly, because of brand-new adherence to the market, its rules are applied more rigidly than in a genuine market society.

i) Unemployment

As pointed out earlier, most state-socialist countries operated as if unemployment did not exist, and consequently they had no provisions for unemployment and no market-friendly solutions to handle it. By 1990, all of them had put into place some form of unemployment benefit scheme, even if they were not very generous and if their rules were so strict as to shut out large categories, first entrants among others. It should be noted that Poland is an exception in this respect (see BIT: *Accords intérimaires*). Also, Hungary has adopted in February 1991 an Employment Act which offers some protection to first entrants and is preparing active labour market measures. However, in most countries of the region a weak and underfinanced passive labour market policy has appeared, without really stopping the hopeless impoverishment of the unemployed. Thus, a weak and underfinanced passive labour market policy is appearing which does little to stop the hopeless impoverishment of the unemployed.

In fact, 'market-friendly' instruments of active labour market policies encounter many difficulties. The encouragement of self-employment is hindered by a lack of funds ? and also by the widespread lack of entrepreneurial know-how. Legislation which encourages, or at least enables a 'social economy' is practically non-existent. Some training and retraining programmes exist practically everywhere. However, because of the great uncertainty about future openings, they may appear absolutely irrelevant and therefore not very attractive.

One instrument often used in market economies is the 'parking' of young people in the educational system until the worst is over. This would be of special importance in the former 'eastern bloc'. However, vocational training has to be radically improved and adjusted to new conditions. The is true of higher education where enrollment has been relatively low in comparison with to western Europe (Kozma, 1990). The situation, furthermore, is expected to worsen between 1991 and 1996 when there will be a substantial increase in the number of young entering the labour force as a result of the pro-natalist policies of the 1970s (Winniczuk, 1990). With the possible exception of Czechoslovakia (see Chapter 6), governments are not planning any serious changes in this respect. This may be because

of the lack of funds, but also because of the continuing devaluation of education, or of the neglect of the young and their needs.

In addition, all suggestions vaguely reminiscent of the 'old system' are rejected as politically suspect. Thus, for instance, it seems to be impossible to defer the lay-off of 'redundant' workers until new openings or other solutions are available. Also, while state-financed social and health services are tragically undermanned, it is anathema to suggest more openings. The real or alleged reason is, once again, scarcity.

Most importantly, many new governments accept large-scale unemployment as an absolute must which cannot be avoided. This is the main cause of the lack of proper efforts. It also acts as a self-fulfilling prophecy. It may well be, as many experts suggest, that massive and large-scale unemployment is, or will be, an inevitability in developed countries. But this does not hold true for the underdeveloped countries of central and eastern Europe. The state of their economies corresponds, at best, to the level of development of the 'post-industrial' countries in the early sixties, when full employment was on their agenda.

ii) Wages and prices

The obvious result of liberalisation in these spheres is that market wages will be very unequal, and in case of very large groups they will not cover the price increases for the most elementary needs. Wage bargaining is hampered in most 'new' countries by the discrediting of all left-wing movements, the obsolescent behaviour of the former trade unions and the weakness of the new ones, as well as by the slow emergence of mechanisms for collective bargaining.

Through fear of spiralling inflation, most governments did not work out a policy to concert wages and prices. While it is widely recognized that the full price of basic needs was not 'included' in the former wage structure, because it was paid for by redistribution, and while this redistribution is slowly abolished, across-the-board or automatic wage increases have seldom taken place.

More generally, the countries in question have not been prepared to face inflation and to devise tools for handling it. Therefore, the indexation of wages and of social benefits (with the exception, to some extent, of Poland) is inadequate.

The political problem of the rejection of everything which seems to be a continuation of the former system is also present here. The shedding of the social load is particularly interesting in case of prices. The current axiom is "that everything has a price to be paid by the user". There may be many reasons — social, political, environmental or economic — for not applying strict market prices which are often used in western countries.

The examples abound from the subsidization of agriculture to that of public transport or housing. In the new democracies though, this flexibility is rejected for fear of the past, because of *true* belief in the market, and, of course, for budgetary reasons. Therefore, in cities already severely polluted, the tariffs of public transport are constantly being increased. So are rents and household energy, with almost no provision for those unable to pay. The social services (from home help to school canteens) which used to operate free, or for a nominal charge, are now introducing full user charges.

iii) Social policy and the new ideology

The promotion of a greater role for market forces proceeds with great difficulty in precisely those spheres where this would be rational and necessary. There are many reasons to this, from the utmost difficulties of dismantling the ownership monopoly of the state and the resistance of well-organized industrial lobbies, to the lack of local capital and the fear of foreign capital. Resistance to (pseudo or real) market solutions is weaker in the field of social policy.

The idea of private and market solutions in health, housing, education, social security, and social services is now widely popular in all ex-socialist countries. It is firmly emphasized that the government is in no position to improve any of the systems. On the contrary, the old system is accused of having overspent on social provisions and of having pampered the population. Therefore, all those who want better (or acceptable) services or benefits are urged to take out complementary private insurance, or to pay for service on the private market. In some countries, private pension and health insurance companies have already appeared, together with private medicine and private schools.

There is a two-fold problem involved here: on the one hand, economists are increasingly concerned with the apparently unavoidable 'market failures' and information failures in these fields (Barr, 1987a, 1987b, 1990). The proponents of market solutions seem to be completely unaware of the new findings of economists. On the other hand, market solutions require solvent demand. With a major decrease in average real incomes and a significant increase in income inequality, this demand will be restricted to a tiny minority. Hence, there will be an almost unavoidable emergence of 'dual systems' in health, education and insurance. The segmentation of social institutions may affect in a negative way social integration which is already in a very sad state in all ex-socialist countries (Ferge, 1991).

One of the most important corollaries is the spreading conviction that

social insurance has to be purified from its non-insurance elements and has to be neatly separated from other social programmes.

In the state socialist countries, the system of social insurance only included social benefits in cash. Universal benefits, such as the maternity grant at child birth, were the exception. Most of the provisions were tied to regular employment. Some of these were flat-rate (e.g., family allowance), but the majority were earnings-related (e.g., pensions, sick pay). The health and education systems were financed from the budget as a public service. Social assistance in cash was the responsibility of local government, as are the newly emerging social services.

This system is undergoing change. The present objective is to make a clear distinction between benefits and services covered from general taxation (the budget), and from contributions by employers and employees (the payroll). In the case of social insurance benefits, the 'equivalence principle' (between contributions and provisions) is to be applied more strictly. This means a weakening of social solidarity and the exclusion from the insurance system of all those who do not fulfill the increasingly stringent conditions for eligibility.

These changes would not create grave problems if the countries in question had decent social security systems. This would imply certain basic (flat-rate) benefits, with clear entitlements, for all citizens, such as a universal basic pension, family allowance for children and a social safety net for the poor and the unemployed. In the World Bank's formulation, this should mean "establishing minimum standards of financial support that are transparent, normative, and widely known, with the assurance that the funding will be available for all claimants who meet the criteria, and with the right to a formal appeals process" (World Bank, 1990).

Unfortunately, a strong market orientation, limited resources and the survival of prejudiced and conservative thinking in social matters point in another direction. A universal basic pension did not exist in the ex-socialist countries and nowhere is its introduction on the agenda. Family allowance has become universal in Czechoslovakia, Hungary and Poland over the last years. But at present, a new debate questioning this arrangement has surfaced in each of these countries, as well as in the Soviet Union. It is argued that funds would be more effectively used if restricted to the truly needy. This means that family allowances should be made selective and reserved for the poor. This proposal is usually made without calculating the extra financial cost of selectivity and does not take into account the very negative social and economic impact of this measure, nor the number of families and children included among the truly needy. In Hungary, for instance, it can be shown that the needy make up an overwhelming majority of families with three or more children, a significant majority of families with two children and a slight majority even in

families with one child. It is highly probable that introducing selectivity and means-testing would cost more in sheer money terms than the sum economized due to this measure.

The number of those needing assistance may, therefore, escalate. Simultaneously, and despite frequent declarations to the contrary, the discretionary character of social assistance does not seem to change. It may even be accentuated if, for instance, social workers were asked to identify the current standard of living, and to assess the needs, of families. As yet, the endeavours to introduce assistance schemes with normative entitlements are scarce. Only Poland seems to have advanced in this direction.

If the current projects materialize, the ex-socialist countries may end up with a large, marginalized population, and with weak, residual state or locally managed social policy programmes directed towards the poor and with divisive market solutions in the field of traditional public welfare.

It is somewhat paradoxical that the ex-socialist countries are taking different directions in different spheres of social life. In the economy and in politics, they try to replace the former command systems, requiring constant deliberate intervention or 'hand-geared' methods, by impersonal mechanisms; the asymmetrical power relations by symmetrical contractual relationships; and arbitrariness by the rule of the law. Meanwhile, in social policy they are reverting to 'hand-geared methods' on a large scale; they are maintaining asymmetrical paternalism; and they are reluctant to base this sub-system on legal entitlements.

It has to be emphasized that nowhere is this outcome deliberately pursued. However, if the present projects and debates are followed to their logical conclusions, this might well be the result. The problem is that if systems of social solidarity are weakening, market solutions are spreading and the instruments of conservative poverty-politics become firmly institutionalized, the countries may not be able to return to less segmented, more participatory and more social frameworks.

3. The trade-offs of welfare politics

The classical trade-off of social policy is between equity and efficiency (Okun, 1975). The terms of this trade-off are now changing: equity, or equality, are seen by many in the former socialist countries as obsolete demands, the enforcement of which has greatly harmed efficiency. It is assumed that efficiency will be enhanced if equity and equality cease to be centrally supported objectives. Many interpretations go even further, suggesting that increasing inequalities are proofs which guarantee increasing efficiency[8].

In the transitional period from state dictatorship to market democracy, the contours of a new trade-off are taking shape, namely between increased freedom (not merely consumer freedom but political freedom in the broadest sense) and decreasing security. While a majority of citizens may be adversely affected economically, many may consider the economic loss worth the political gain. Opinions will differ widely. Those groups which become hopelessly impoverished, unemployed, homeless or destitute will not appreciate the new freedoms. But, as usual, they will not be very vocal or well organized, at least for some time to come. However, if the losses are too big and the compensations too meagre, the unorganized losers may become a politically destabilizing force or, in the most pessimistic scenario, may become a threat to the new democracies.

III. Is there another option?

If one takes into account the state of the economy and those forces currently engaged in restructuring, a generous or even a satisfactory social security system is unlikely to emerge in the new democracies. The dominant political forces have not yet formed a comprehensive or longer-term view of the welfare politics. Rather, emergency measures, a safety net based on social assistance, private and voluntary solutions and piecemeal reforms are the imminent items on the agenda. This is clearly the case with the three-year programme of the Hungarian government (A nemzeti megujhodds programja, 1990). It may be worthwhile to think about alternatives.

1. The long-term view

If one disregards the prevailing political forces and economic conditions, a combination of the Swedish and Finnish systems would be the ideal solution. This recipe includes: active labour market policies and a (not very widespread) "social economy", which guarantee employment for almost all; a generous wage policy containing wage inequalities although ensuring decent wages to all; universal benefits which also profit the middle classes thus making it almost pointless to look for private arrangements; firmly guaranteed social rights which ensure help without stigma; participative practices in shaping the welfare system both at national and local level; affirmative action in favour of vulnerable groups; social initiatives which articulate new needs; and a responsive state to support them. In short: a participative system with democratic controls which is given a mandate through through accepted political mechanisms, and which aims to reconcile freedom, equality, solidarity, tolerance, humanism, and if need be, altruism. If unemployment cannot be contained, this arsenal

could be completed by a so-called basic income scheme which has been debated in countless western papers and books over the last years. (Atkinson, 1987, 1990a, 1990b; BIRG, 1989; Offe, 1987; Przeworski, 1986; Roebrock, 1988; Van Parijs, 1990; Vobruba, 1990a; Walter, 1989). The basic income, an unconditional universal flat-rate minimum, may simplify all other income maintenance programmes and may end the worst aspects of stigmatizing and divisive social assistance programmes.

The renewed appeal for this relatively old idea is due firstly to the fear of lasting mass unemployment. The second reason is the fear of an impoverished social policy emerging from the current preparations for an integrated Europe. Of course, the political resistance may be tremendous, but this is no reason for dismissing the whole idea too rapidly.

However, a welfare society combining and bringing to perfection the best elements of Swedish, Finnish and basic income policies is clearly a long-term view of welfare politics. Its details are not too difficult to work out on paper and there are many attempts in this direction (see Ferge, 1990). However, this is not the place for a detailed description of such a far-away project — all the less so if there are no political forces behind it. And while — according to the results of various surveys — a majority would be in favour of a welfare model offering security in conformity with human dignity, the politically institutionalized forces are not contemplating such dreams.

In fact, the new governments (and the new parties) of the former state socialist countries seem to be, as yet, unable to take a longer-term view. The economic situation and the political struggles are devouring all the available energies. The present-day reality of central and eastern Europe is too far removed from any utopian recipe, most probably more for political than for economic reasons.

The lack of long-term thinking may be detrimental also for short-term projects. Many measures may be introduced on an emergency basis; but without proper safeguards, they might easily become rigidly institutionalized.

2. Handling the crisis

The situation has already deteriorated so far as to warrant huge efforts in the immediate future. The most important immediate task seems to be the handling of the crisis. Therefore, it is necessary to concentrate on those practical proposals of crisis management which look for solutions which will not hinder change once the crisis is over.

The major problem right now is the growth of absolute poverty, especially the homeless, the unemployed, the low paid, a part of the elderly and the majority of families with three or more children. These

groups make up at present — in Hungary for instance — about 2½ million persons (25% of the population)*. One-half are under the poverty line, and the other half are hovering around it. In Czechoslovakia, the situation may be somewhat better; in the other countries, it may be similar or worse. In many of them (Bulgaria, Romania, the Soviet Union) dire shortages of basic needs and a system of rationing (food coupons) have already been put in place.

There are no optimum solutions to these problems, only emergency ones. The priorities may be different in each country. The following checklist relates only to Hungary, but it is probably not radically different from the situation in other countries (in order to understand the estimates below, it may be useful to mention that the population of Hungary is 10 million and the GDP in 1990 is estimated at 2,063 billion forints, or $33 billion.

— Shelter could be provided by evacuated military buildings (especially those left by the Soviet army in many towns) and emergency buildings could be used for this purpose. Buildings far removed from towns are useless, because no jobs would ever be available there and the homeless would be entirely deprived of social contacts and possibilities of reinsertion. The homeless and the unemployed could be organized, with the proper guidance, to repair or reconstruct the buildings. While local authorities should be responsible for solving this problem, the organizers should belong to non-governmental movements as the State's methods, even at local level, are not likely to change fast: these could easily anger or alienate the people. The funds should be assured by the budget, and the wages should be living wages, thus breaking with the age-old tradition of low wages in 'workfare', through jobs created purposefully for the unemployed poor.

The estimated total cost for an estimated total of 30,000 homeless, and using the cheapest possible solutions, may be around 20 billion forints (deducting the saving made on unemployment benefits, but not counting other, more long-term economic gains). This is about 1 per cent of GDP.

— Prevention of loss of home because of inability to pay the rent, the increased interest rate or household energy (utilities). The instrument, akin to the one proposed in Poland, is a means-tested housing allowance if housing costs (including utilities) exceed a pre-determined percentage. According to the estimates of the World Bank for Hungary, if market prices are introduced, about 250,000 families might need this allowance. (In Poland the housing allowance is granted to those whose housing expenditure exceeds 8% of their monthly income, under certain conditions.)

The estimated cost in Hungary would be (again, in the World Bank's estimate) 7 billion forints a year, if the accepted ratio is set at 20 per cent

of the household's income. In these estimates the increased state revenue would far exceed the subsidy. In any case, the allowance should not be — even at full market prices — more than 0.5 per cent of the GDP.

— Stop hunger thanks to increasing numbers of meals served at an increasing number of the Churches, the Red Cross and other benevolent groups. The local authorities should guarantee this provision with centrally assured funds, even if voluntary agencies continue to play a role. But they are not present everywhere, and they cannot always guarantee provisions. The estimated cost should not be over 1 billion forints, a tiny fraction of GDP.

— Prevention of undernourishment of children could be ensured in different ways: as school meals are already established, they should cost only a nominal sum for all children and provided free for families with several children and single parents. This is an emergency situation. If the quality of the meal is improved — which is a must — the market price will become prohibitive for most parents. The abolition of income-tested fees for school meals in the last years has already led to many children being excluded from school meals.

The total estimated cost for all children between 3 and 10 (numbering 900,000 in 1990) would be about 18 billion forints (counting with 200 meals per year per child). This is less than 2 per cent of the GDP, and could be reduced, for instance, with some co-payment, at least in the case of families with one child or two children. The real cost may be less, if, as in the past, a proportion of teenagers do not eat at school.

Another instrument against undernourishment could be the food stamp as it is used in the United States. This would be an urgent multi-purpose programme: because of diminishing solvent demand, agricultural production is declining and the future is threatened (as the milk cannot be sold, cows are killed, etc.). Food stamps have never been used on a large scale in the ex-socialist countries, but similar instruments are not totally unknown. For instance, most of the countries, at one time or another, have had milk stamps for children, entitling them to cheap milk.

It is hard to cost such a programme. If, for instance, a universal food-stamp programme for all children were to replace the next two cash increases of the universal family allowance, with half of the subsidy withdrawn from milk production added to this sum, it would amount to about 10 billion forints (or 0.5% of GDP) without additional extra costs to the budget (note that this programme should also be available to pensioners in need).

Other help for families with children might take the form of the French system (a variation of the food stamp, though not for food). This provides reductions for all sorts of goods and services (children's clothes, shoes, transport) to families with more than three children. Unlike

France, however, where the adult members of the household are also the beneficiaries, only children should benefit in poorer countries. The first move in this direction has already been made: Hungarian Railways restored cheap fares for large families as from January 1991. The total estimated cost (for about 400,000 children) is around 2 billion forints (or 0.1% of GDP in Hungary).

These, and other, emergency measures would operate only if minimum wages and minimum pensions reached the poverty line, and if most social benefits are indexed. Otherwise, the need for social assistance will be very high indeed, thus creating bottlenecks, extra work and lots of bureaucratic red tape and humiliating practices.

The problem of low wages cannot be directly handled by the state under conditions of a market economy. Legislation about the minimum wage is possible (and usually does exist), but with high unemployment rates heavy bargaining will be needed if the minimum wage is to reach the poverty line. Even in this case there is a high possibility that employers will underbid the minimum level, and the employees will accept wages lower than the legal minimum. The importance of family allowance and of targeted assistance is increased just because of the high probability of low wages.

The cost of assuring a low, but acceptable minimum pension to all above the pensionable age limit would amount to about 12-15 billion forints at 1990 prices.

It is worth mentioning that estimates have already been made to calculate the potential demand for social assistance using the concept of the 'poverty gap', namely, the total amount of money that would be needed to raise the poor just above the poverty level. According to data from the incidence study undertaken by the Hungarian Central Statistical Office and sponsored by the World Bank, the poverty gap in 1989 amounted to 10 billion forints (0.6% of the then GDP). This is a much lower sum than the one necessary to increase minimum wages and pensions, because it concentrates only on poor families. However, it does not count the costs of introducing a system of means-testing. On the other hand, the World Bank expects a heavy rise in the poverty gap in the coming years.

According to the estimates presented above, the cost of the emergency measures, including some with preventive elements, would amount to about 70 billion forints, one billion dollars. Together with the costs of unemployment, the prevention of harsh impoverishment would cost no more than about 5 per cent of GDP.

This sum looks prohibitive if seen from the perspective of already highly pressed finances. The budget for 1991 makes provisions for far less than this amount. All further needs have been ignored by the Parliament

because the budget deficit was considered taboo, and strong interests opposed other cuts.

However, the sum is amazingly low if seen from a wider perspective. If dire poverty can be prevented with an outlay of only 5 or even 10 per cent of the GDP of a country, this means that the issue is not altogether impossible to resolve. This was certainly not true for pre-war Hungary, and may not be the case in many Third World countries. The difference is that many of those currently poor are the 'new poor', who have a relatively solid background and who are not too far below the poverty line. The problem is that if preventive measures are not taken in time, then the situation of those now sliding into poverty will rapidly deteriorate — so that the efforts needed for restoring their former status will cost much more. (They might lose their home, sell their goods, lose their health, etc.). That is why a longer view is essential even in handling the emergencies.

While part of the missing sum could be obtained by making various cuts in the budget, the issue is, ultimately, not financial, but political. As long as the elementary needs of people, and especially children, are not given higher priority by policy makers, there is no way to prevent their pauperization.

NOTES

[1] I have to thank Giovanni Andrea Cornia, John Micklewright and Sándor Sipos for their helpful comments on the first drafts of this paper.

[2] Child-care arrangements are not taken into consideration. As a matter of fact, state socialist countries fared better in this respect than market societies (Kahn and Kamerman, 1981).

[3] In fact, Hungary appears in the U.S. publication for 1985 as having unemployment assistance based on a law of 1957, and in the volume for 1987 as having an unemployment assistance programme based on a law of 1986. In fact, the conditions offered by the 1957 law were so bad that, from the sixties on, when open unemployment was gradually phased out, this piece of legislation was defunct: nobody ever asked for it and nobody was ever granted it (the majority of municipal councils, when explicitly asked, did not even know about it). The law of 1986 was not a genuine unemployment assistance scheme. It only lengthened the period of the paid layoff. The first genuine unemployment benefit scheme was introduced only in 1988. Of course, one does not know how many countries have 'cheated' in reporting to the ISSA or to the ILO in this way.

[4] Information given by Dr. Piotr Mierzewski at a seminar held at the International Child Development Centre, Florence, in January 1991.

[5] The number of unregistered unemployed is a rough guess. The figures are partly based on the estimates of the labour exchange offices which do not register first entrants. Many hopeless job-seekers, not entitled to benefits or sure of not getting any offers, avoid

them. The above guess covers also those who have more or definitively withdrawn from the job search, because of having given up hope entirely.

[6] Information given by Alena Kroupová at the ICDC seminar in January 1991.

[7] In Hungary, for instance, the first 'package' of instruments to fight unemployment included cheap loans to enable the setting up of new ventures. This instrument was withdrawn essentially because of lack of funds. The alleged reason was that these loans were not used by the truly needy, but by shrewd businessmen.

[8] It is largely unknown in this part of Europe that the soundness of the assumptions about equity/efficiency trade-offs is currently being questioned by economists themselves (Atkinson, 1990).

[9] Estimates of the Central Statistical Office, based on the income distribution survey of 1987, and of the prevailing trends since then in price rises, wage changes, etc.

CHAPTER 4

ECONOMIC REFORMS AND CHILD WELFARE: IN PURSUIT OF ADEQUATE SAFETY NETS FOR CHILDREN

Giovanni Andrea Cornia

Introduction

The transition by the countries of central and eastern Europe to democratic pluralism and the market economy can certainly be considered one of the most important political, economic and social events of this century. Its potential benefits are immense and likely to extend well beyond the population of the countries directly concerned. Great hopes are therefore being fueled by this historic occasion to start anew.

Because of the immensity of the changes it implies, the transition to the market economy poses, however, a number of important challenges which affect practically all aspects of life. In the social sector, the transition to the market economy requires three different but closely interrelated problems to be tackled simultaneously. First of all, there is a need to fulfill the expectations about the elimination of the shortcomings, distortions and injustices inherited from the socialist regime. Second, 'safety nets' must be put into place rapidly to deal with the largely unavoidable social costs arising from the radical economic reforms initiated in Poland, Hungary and Yugoslavia in late 1989, and which are still underway in most of the region — and likely to grow in importance in the Soviet Union in the near future. And third, social policy has to be adjusted gradually to meet the new economic conditions.

To a considerable degree, the solution to these three problems depends on the speed, extent and pattern of economic recovery in the region. Decisions about safety nets and social policies can, however, contribute in a major way to the achievement of these objectives and to the success of the reforms by strengthening the human capital and by providing the necessary social consensus to the new policies. The need for an adequate social policy is even more evident in the case of vulnerable groups, of which children, adolescents, single parents and the elderly

constitute the largest group. It would be ethically unacceptable and economically inefficient to try to solve economic problems at the expense of any one of these groups.

I. The Crisis of the Socialist Model

1. Economic and social decline

The stagnation or decline of most indicators of social welfare during the last years (see Chapter 1) is probably the most conclusive sign of the failure of the socialist experiment in the countries of central and eastern Europe. The decline in economic performance, which affected all countries of the region without exception, became evident after the first oil shock, gradually intensified over time and reached unmanageable proportions towards the end of the 1980s (Table 4.1). In the relatively simple

Table 4.1 *GDP growth rates*

	1950-73	1973-82	1982-88	1989	1990	1991
Soviet Union	5.0	2.1	1.9	2.5[1]	—4.0[1]	—
Bulgaria	6.1	2.4	1.4	—0.2	—9.5	—5.7
Czechoslovakia	3.8	1.8	1.8	1.0	—1.3	—1.9
G.D.R.	4.6	2.6	2.1	—	—	—
Hungary	4.0	1.9	1.4	—1.2	—8.2	—5.0
Poland	4.8	0.5	4.2	—1.6	—18.4	—4.3
Romania	5.9	3.7	2.5	—3.1	—18.6	—3.6
Yugoslavia	5.7	5.0	0.9	—1.0	—9.1	—5.8

Source: For 1950-88, Maddison (1989); for 1989-91, Robinson (1991); IMF, *et al.* (1990).
Note: [1] NMP growth rates.

economies of the 1950s and 1960s, the centralised command structure had been able to achieve significant 'extensive growth' and some increases in basic living standards and social conditions. Performance started to deteriorate gradually, however, when the extensive supply of labour (from rural areas, from the incorporation of women in the labour force and from population growth) began to dwindle and when an increase in the rate of innovation, technological progress and microeconomic efficiency became necessary to sustain output growth. It is true that some slowdown in the rapid pace of growth in the 1950s and 1960s was inevitable, and that the two oil shocks of 1973 and 1979 caused terms-of-trade losses to all countries of the region except Poland and the Soviet Union. It is true also that poor weather conditions affected agricultural performance in the 1970s. The main cause of the poor performance of central and eastern

European countries is to be found, however, in the rapidly increasing technological, information and incentive difficulties faced by central planning when the scale and sophistication of the economy grows. As complexity grew, microeconomic efficiency declined and overall growth slowed down.

Although many of these difficulties were well known, policies contributed little to ease the problem. Except in Hungary, which adopted some timid reforms, no major changes in economic policies were introduced during the 1970s and 1980s to ease the growing inefficiencies and tensions which were emerging. By the late 1980s, a radical reform of the economic system had become therefore unavoidable.

2. Social policy crisis

The poor performance of the economy since the early 1970s represented a major obstacle to the improvement of standards of living, to the extent of redistribution and to the enhancement of social policy, as illustrated most vividly by the sorry state of health services and social assistance throughout the region. Stagnant living conditions were also the result of systemic biases affecting social policy which — quite independently of economic factors — reduced its overall effectiveness, the quality and relevance of public services and the ability of public administration to respond to the real needs of the population. Such biases (which are discussed in greater detail in Chapter 3 and in the four national case studies which form a part of this study) were the result of ideological factors, lack of incentives, poor management, excessive centralisation and substantial inequalities in access to public services. Among the first, the alleged primacy of 'productive' over 'non-productive' activities deprived public services of adequate human and financial resources. In addition, the alleged superiority of state ownership prevented any meaningful development of complementary private welfare services.

Second, inadequate incentives, poor management and excessive centralisation led to inefficiency, wastefulness and diversion of funds. In addition, the centralisation, paternalism and lack of popular participation of socialist social policies engendered a strong sense of passivity, dependence and cynicism in the population and reduced their self-reliance and sense of responsibility and initiative. In the field of social security, for instance, the *de facto* confusion between Social Insurance Funds and the state budget often diverted resources to non-social insurance purposes. Third, in spite of the proclaimed universal free access to public services, substantial differences existed, for example, in access to health care,

education, housing or recreation. While the *nomenklatura* had privileged access to elite services, travel abroad and parallel distribution systems, the bulk of the population had to bear substantial hidden charges in the form of gratitude money for services they were in principle entitled to free of charge (Csaszi, 1990).

Socialist social policy led also to the weakening of the role of the family in child socialisation and education, and to the growth of 'social orphans' (i.e., children with very limited or no interaction with their parents). Among the factors responsible for this situation were: the necessity of relying on two full-time salaries to ensure adequate living conditions; the erosion of the nuclear family and the weakening of the extended family; and the strong role advocated by the Party-State in child socialisation.

Despite these serious handicaps, which are being addressed by the reforms underway, social policies in central and eastern Europe have been characterised also by a number of positive features which it is hoped will be retained in the new social architecture. Among them are:

— The priority accorded to social expenditure in the state budget. With the exception of social assistance and health services, the other components of social expenditure have consistently received a share of national resources commensurate to that of the western industrialised countries. This allowed the provision of universal benefits and services which, despite widespread problems of efficiency, poor quality and unequal access, were widely available. Cash benefits accounted for almost the same proportion of national income than in western industrialised countries, while similar conclusions hold true for government expenditure on education and social amenities. This is a relatively important feature in view of the substantially lower income level of the socialist countries (estimated by the World Bank at $2,000-5,000 per capita). In addition, the population benefited from large subsidies on food, other consumer goods, housing and public transport which, while distorting the price structure and draining budgetary resources, constituted an important component of real household income.

— Child and family policy was particularly comprehensive in terms of the range and generosity of the benefits provided. The basic scheme generally included maternity leave and benefits, childbirth grant, child-care leave, child-nursing benefits and generous universal child allowance. The child allowance was particularly important and absorbed a share of national income higher than in Germany, Sweden, the United States (the three countries used as models in Chapter 2), Portugal or Greece (which had roughly similar GDP per capita) and of the OECD average (Table 4.2). Only in France, where child allowances have been the most comprehensive and generous for a long time, was such proportion higher. Because

TABLE 4.2 *Expenditure on child/family benefits as a share of NMP or GDP*

	1980	1985	1989
	A. *Shares of NMP*		
Bulgaria	3.3	3.3	3.6
Czechoslovakia	3.8	3.9	3.6
Hungary	3.2	3.2	4.7
Poland	1.1	2.1	2.3
Soviet Union	0.6	—	0.9 [3]
	B. *Shares of GDP*		
United States	1.0	0.8 [1]	—
Germany	1.9	1.3 [1]	—
Sweden	3.1	2.2 [1]	—
France	4.5	4.8 [1]	—
Greece	0.6	0.6 [1]	—
OECD Average	2.6	2.4 [1]	—

Source: Panel A (except USSR) - Czechoslovakia, Hungary, Poland: Chapters 4-8 of this volume; Bulgaria: BCSO (1990); Soviet Union: Goskomstat (1989a, 1989b); Panel B - Varley (1986).
Notes: [1] 1984; [3] 1987.

of this, Hungary and Czechoslovakia, in particular, have been singled out — together with Sweden, Norway and France — as the countries with "an explicit and comprehensive family policy" (Gordon, 1988, p. 22). In terms of the average wage in manufacturing, child allowances in families with two children were much larger in central and eastern Europe than in any other OECD country, while for a four-child family, only France had allowances larger than Hungary and Czechoslovakia (Table 4.3).

TABLE 4.3 *Family allowances as a percentage of average wages in manufacturing for families in selected countries, 1985 (basic system only)*

	Two Children	Four Children
Czechoslovakia	22.6	59.7
Hungary	16.8	39.5
United States	0.0 [1]	0.0 [1]
Germany	4.3	14.2 (or more)
Sweden	9.4	25.9
France	9.5	64.3
Greece	5.1	13.1
OECD Average	—	—

Source: Gordon (1988), Table 13.1.
Note: [1] In the United States, in 1985, there was no universal child allowance.

— In particular, child benefits were of crucial importance for families which had more than two children or which faced multiple risks (single parenthood, handicaps, very young parents, etc.). Child and family benefits accounted for between one-third and one-half of the total disposable income of single-parent families, families with three or more children, families with handicapped children or with only one breadwinner in a low-paying job. Such family benefits have therefore avoided severe deprivations for these types of families and functioned fairly well from the perspective of poverty alleviation.

— Child-care services were particularly extensive. Enrolment in crèches and, in particular, in kindergartens was very high, particularly in comparison with most of the OECD countries. At the end of the 1980s, for instance, enrolment in pre-school education for 3-6-year-old children was 97 per cent in Czechoslovakia and 87 per cent in Hungary. While this was, in part, the outcome of the high rate of participation of women in the labour force, it certainly had a positive effect on children, whose proper development was also shown to depend on continued interaction with other children and appropriate forms of stimulation.

II. Economic and social reforms and their short-term impact on children

1. Economic reforms

Between 1990 and 1991, the countries of central and eastern Europe introduced simultaneously three types of reforms, namely, macroeconomic stabilisation, microeconomic and sectoral restructuring, and privatisation.

Macroeconomic stabilisation aims at eliminating the government budget and balance of payment deficits and at controlling inflation (under the form of *open inflation*, as in Poland, Hungary and Yugoslavia, or *repressed inflation* as revealed by widespread shortages, huge monetary overhang and grossly undervalued currency in parallel markets, as in the Soviet Union, Czechoslovakia and Bulgaria). Stabilisation includes *demand-restraint* measures such as tight monetary and fiscal policies and wage control aimed at curtailing domestic aggregate demand and imports. This entails, in particular, large public expenditure cuts achieved mainly through the elimination of producer and consumer subsidies (such as those envisaged in Bulgaria in the 1991 budget, equal to 23% of GDP). Stabilisation also comprises *supply-enhancing* measures such as exchange rate devaluation, interest rates, product pricing and policy to enhance factor mobility, as well as *institutional reforms*, in the areas of foreign trade, taxation and others. The problems involved in trade reform are particularly difficult for the central and eastern European countries which have to redirect,

almost at once, a large share of their export to countries outside the former CMEA group. Despite large devaluations, which improve the competitiveness of domestic production and exports, changes in tariff and non-tariff protection and export subsidies might therefore have to be put into effect more gradually to avoid a sudden collapse of domestic industry.

Microeconomic and sectoral restructuring aims to shift resources towards those sectors with unsatisfied domestic demand (such as consumer durables and services) and away from heavy industry (particularly steel-making, shipbuilding and machinery). It also aims to channel resources to activities with lower opportunity costs, in terms of energy intensity (Poland, for instance, is the most energy-intensive country in the world) and environmental degradation, and to activities embodying best practice technology and with potential for exports on the world market.

Privatisation, the most ambitious and complex component of the overall reform, aims at establishing new forms of ownership (private enterprises, cooperatives, joint ventures and foreign companies) and new 'rules of the game' in terms of price formation, bankruptcy, competition, credit and financial markets.

To support the reform process in the above three areas (and in that of privatisation in particular), a major recasting and upgrading of the legal and institutional framework is necessary. This new framework, which is crucial for the smooth functioning of a market economy, requires:

— Major amendments to the legal system, including the revision or abrogation of existing laws and regulations and the approval of new ones, particularly in the field of privatisation, foreign investment, restitution of nationalised property, bankruptcy, anti-trust and competition, capital markets and banking, taxation, unemployment and social policy, and family and social assistance.

— The building of new institutional capacities to ensure the application of the legal provisions illustrated above. This requires creating capital markets, employment offices, regulatory and surveillance bodies, and the strengthening and expansion of weak existing public structures dealing with taxation, public assistance, commercial banking, etc. In addition, new skills in management, accounting and various technological branches need to be developed.

— The allocation of adequate financial resources for the building up and functioning of these public institutions.

2. Problems associated with the economic reforms underway

There is little doubt that the above policies are necessary, that they will likely lead to marked rises in the standard of living, and that without them the central and eastern European economies would be condemned to

an endless stagnation. Because of their unprecedented complexity, however, such policies face important difficulties which may slow their implementation, produce a negative impact on human welfare, and require much broader safety nets to prevent undeserved massive pauperisation.

Although macroeconomic stabilisation, privatisation of state-owned companies and other economic and social reforms have been fairly common in both developed and developing countries, particularly during the last ten years, the complexity of the task faced by the countries in central and eastern Europe is simply daunting. There are no historical precedents of countries aimed at achieving, simultaneously, the three objectives illustrated above. In addition, even for each of these three reforms, there remain unanswered problems. To start with, while economic and political conditions in central and eastern Europe are substantially more favourable than in most developing countries, the debate on stabilisation and structural adjustment in resource-constrained economies is far from concluded. Broadly speaking, the monetarist approach to macroeconomic stabilisation in economies affected by a severe shortage of external financing has, in most cases, achieved the objectives of controlling inflation and reducing the budget and balance of payment deficits, but at the cost of sharply curtailing investment, growth and welfare. This situation contrasts with the post-war experience of the then Federal Republic of Germany in which the success of a drastic stabilisation and currency-substitution programme was facilitated by abundant external resources and a positive industrial policy.

Similarly, although privatisation efforts have been underway in the 1980s in many industrial market economies and developing countries, the numerous steps implicit in this process (such as some industrial restructuring, the evaluation of assets, the flotation and placement of shares, etc.) have required considerable time and resources. Even in the United Kingdom, for instance, the country which pursued this policy the most actively, only a relatively modest share of state-owned industrial assets was effectively privatised in the 1980s.

In addition, the legal changes and building of institutional capacity would entail collapsing in a few years a long series of steps which required several decades, or more, to build in the OECD countries.

From the perspective of the impact on the distribution of income and human welfare, the policy reforms underway suffer from a number of problems which could threaten the preservation of minimum living standards, a socially acceptable income distribution and undermine, or at least delay, the achievement of macroeconomic balance and rapid growth under free market conditions. Among these problems, the three main ones are discussed hereafter.

The pace and sequencing of the reforms

While a rapid move to 'true' prices and more sustainable deficits may be desirable from a monetary perspective, large and sudden changes in absorption, price levels and relative prices may entail a huge drop in economic activity and, in the absence of broad safety nets, important welfare losses. In addition, drastic measures in the field of devaluation, the removal of subsidies and price liberalisation (particularly if in the presence of large monetary overhang as in the Soviet Union) tend to generate strong inflationary pressures which may not be sufficiently offset even by stringent monetary and fiscal policies. This could result in protracted inflation. Some countries, such as Czechoslovakia, have chosen a more gradual approach, particularly in the field of price liberalisation, by spreading the price increases and the fiscal austerity over a longer period of time.

In the view of several commentators (Nuti, 1991), the real question is not so much the pace of economic reforms, but their sequencing (i.e., the order in which policy measures and institutional changes might be best taken during the transition to the market economy). According to some, the disappointing results of economic reforms in Hungary, Poland and Yugoslavia have been due to the overriding emphasis on radical economic stabilisation and price liberalisation measures before key structural and institutional reforms were ready to be implemented (*IMF Survey*, 7 January 1991). Among such key institutional reforms which ought to be carried out before a 'big bang' privatisation and price liberalisation is implemented, the creation of a capital market, the establishment of a tax system and internal revenue service, and the introduction of anti-trust and bankruptcy laws have been singled out as the most urgent. Indeed, the lack of capital market and the obsolete and inefficient commercial banking system inherited from the socialist regime represent a major obstacle to the financing of capital investment and operational needs of new firms. Similarly, in the absence of a rapid and profound tax reform, a major drop in government revenue and further expenditure cuts become unavoidable in the event of privatisation or closure of state enterprises (*IMF Survey*, 4 February 1991). Last, the breaking up of state monopolies and approval of anti-trust legislation would prevent the creation of inefficient private monopolies unchallenged by the competition of other producers, as illustrated, for instance, in the Czechoslovak case study (see Chapter 6).

While the debate on sequencing goes on, there seems to be some agreement that a shock therapy which attempts to tackle, simultaneously, stabilisation, microeconomic restructuring and privatisation is dangerous. It is impossible to solve all of these problems in such a short a time (Nuti,

1991). There is also agreement that it would be naive to believe that privatisation might automatically bring about a positive supply response to contribute to self-sustaining stabilisation. There is, however, some consensus that domestic stabilisation should come first (either as a single package or as a rapid sequence of steps), followed by the establishment of an appropriate institutional framework and new rules for a market economy. Only then could privatisation and, later on, trade liberalisation be introduced more extensively.

The risk of stabilisation 'overkill'

The distorted price and subsidy structure, huge monetary overhang, and, in some cases (such as Poland and the Soviet Union), the large budget deficits financed through monetary creation prior to reform meant that stringent monetary and expenditure policies (and large changes in price levels) were largely unavoidable. These measures are designed purposely to curb aggregate demand and to increase supply so as to bring the consumer market, the state budget and the balance of payments into equilibrium at prices reflecting effective scarcity. However, it is well known that the contraction of demand takes place much more rapidly than the increase in supply (which requires total factor mobility, lack of institutional barriers, fresh capital, etc.). This may lead to an excessive contraction of output and to massive under-utilisation of capital, labour and foreign exchange resources, a huge contraction in household income and consumption, and to a lack of effective demand in the economy. As the experience of Yugoslavia, Hungary and, in particular, Poland shows, real output and income have dropped far more than the targets set by the respective adjustment programmes, while unemployment, idle capacity and trade surpluses have grown substantially, which indicates an under-utilisation of production factors far greater than expected or desired. At the same time, the drop in real income (which was greater than expected) has led to a sharp decline in aggregate demand which left part of the increase in the supply unsold. It would appear from the Polish experience that the 30 per cent decline in industrial production which occurred in 1990 would hardly have been acceptable if the stabilisation had been successful in terms of controlling inflation, eliminating the most inefficient enterprises and achieving the desired restructuring. As these results were only partially achieved, or not at all, the deep recession brought about by the policy reforms was ineffective and socially disruptive (Kolodko, 1990).

While the complexity of the reforms underway should not be underestimated, it is obvious that stabilisation overkill implies considerable social costs in the short and in the long term.

The relative neglect of safety nets and social policy

By and large, social policy and distributive issues have been marginal topics in the debate on the transition to the market economy. In spite of the growing difficulties encountered by the economic reforms and of the pressures of national groups and international organizations (such as the World Bank and the World Health Organization), it has not been uncommon for new social policy to pay only little more than token attention on how to prevent poverty, unemployment and homelessness, or to the preservation of the health and general well-being of poor children and other marginal groups. Instead, the accent tends to be put on 'responsibility' and 'self-reliance' rather than 'solidarity'. This ignores the post-World War II experience of most western countries whereby personal freedom and social solidarity have been reconciled and where economic efficiency has been the result of substantial public investment in human capital and of a broad-based political consensus resting on a fairly equitable distribution of income and on a well-developed system of social security. As a result of this relative neglect, limited resources have been focused on the creation of adequate safety nets, or on the establishment of a new model of social policy characterised by minimum universal provisions.

Several factors might have contributed to the relative neglect of social and distributive issues. First of all, the euphoria engendered by the rapid political changes of 1989-91 which marked the long-awaited beginning of political pluralism and the optimistic expectations accompanying the initial phase of the economic reforms have most likely led to an underestimation of the difficulties implicit in this process, of the social impact of the economic reforms and of the need for adequate safety nets and corrective measures.

Other less contingent factors may have influenced such policy stances (Atkinson and Micklewright, 1991). Among these, the belief that distributional and social performance is to be judged not on, say, the actual well-being of the bottom 25 per cent of the population, but rather on the choice of a form of economic organisation — such as the free market — which is seen as being ethically superior and socially desirable. Another justification for the relative neglect of social policy rests on the conviction that the best strategy for poverty alleviation is rapid growth, the benefits of which will eventually trickle down to all members of society, thus making social policy and redistribution largely unnecessary. Such a view, however, is contradicted by substantial empirical evidence from both developing and developed countries. Finally, the view that, however desirable, social policies and redistribution are inefficient may also have reduced their relative importance. This argument — which is contradicted

by the evidence discussed in Chapter 2 — assumes particular relevance in the former socialist countries currently characterised by a strong backlash against state involvement in any sphere of life. As suggested in the Polish case study (see Chapter 8), as 'socialist' is a discredited word,'social' is also suspect, and even 'public' sounds dubious.

3. Social policy reform and the introduction of safety nets

Changes in distributive and social policies, though profound, have been less drastic than in economic policy. To a considerable extent, such changes reflect the need to remedy the problems caused by the previous regime and to adjust social policy to the new economic conditions. To some degree, and with important variations from country to country, such changes also reflect the spread of neo-liberal views which grant a greater role to market forces in the field of health, education and social insurance, and a 'residual' role to public policy which ought to concentrate on the provision of services and benefits only to those who are unable to secure them on the open market.

Emphasis is therefore put on the principles of greater self-reliance, personal initiative, differentiation of and competition among service providers, efficiency, decentralisation and democratisation, and more generally on a greater sense of responsibility by the individual for his or her life and family.

Emerging trends in social policy

Employment, wages and consumer subsidy policies have undergone radical changes. The policy of artificial full employment has been abandoned and unemployment has been allowed to increase rapidly. All countries of the region have introduced some form of unemployment benefits, with stricter eligibility requirements, shorter duration and substantially less generous benefits than in most western countries. Active labour market policies have been little developed. Wages are less set centrally and are more market determined through various forms of tripartite negotiation. Some countries have introduced minimum wages (calculated in relation to an absolute poverty line and representing, in early 1991, 35% of the average wage in Poland and about 40-45% in Czechoslovakia), while restrictions on wage increases in the public sector have been introduced as part of the stabilisation package. For these reasons, wage differentials may not increase much over the short term, at least in the still dominant public sector. In the long term, however, the wage spread is expected to increase

as wages become more closely linked to performance and wage discrimination (e.g., in the service sector) or preferential treatment (e.g., in metallurgy) will be removed. A wage policy which emphasizes performance may generate positive incentives to work. However, under conditions of high unemployment, passive labour market policies and unequal access to higher skills and education, it may lead to excessive inequality.

All countries have introduced some form of partial indexation of wages, pensions and benefits. The frequency and degree of indexation chosen can cause, however, an extremely large loss of income, particularly in periods of high inflation. Except for Poland and Bulgaria (which has now introduced automatic quarterly indexation, carried out *ex-ante* on the basis of 'expected rate of inflation'), most of the countries of the region, including the Soviet Union, have opted for *ad hoc* compensation for price increases, particularly on the occasion of the withdrawal of consumer subsidies (mostly on food, transport, energy and housing). In most cases, however, such compensation has generally covered only a modest part of the price increases, as, for instance, in the Soviet Union in 1991.

No major structural changes have yet occurred in public services in the areas of health, education, child care and other social amenities. All these sectors have, however, been affected by the decline in government expenditure caused by overall fiscal austerity and by the introduction of substantial user-fees (as for kindergarten meals, school books, drugs, etc.), generally introduced by local governments to compensate for the decline in central government funding. Nominal fees were introduced also with the purpose of increasing efficiency in the utilisation of public services. In parallel, important efforts are underway to decentralize some of these services, as well as social assistance, to the local authorities, while the obstacles to private provision (particularly important in the case of education) have been removed.

Further reforms are being envisaged in the health sector. In many cases this means shifting from a National Health Service-type of health system to compulsory employment- and income-related health insurance, such as those operating, for instance, in Germany and Austria. The supply of health services might also be reformed, with the intention of increasing competition among and the diligence of care providers. One of the options (proposed, for instance, in Poland) focuses on the introduction of 'managed competition' among care providers (such as family doctors and self-governing hospitals).

The system of social security has not yet undergone any major change, although the overall direction of the reforms is clear. In this particular case, there is a move towards a model (similar to that in Germany) based on compulsory employment- and income-related social insurance (for old age, invalidity and survivor pensions, sick pay, unem-

ployment and, in some cases, maternity benefits) administered by an independent insurance fund, fed by the contributions of employees and employers and, for the self-employed, by voluntary contributions. The new system puts more emphasis on the principle of equivalence (between individual contributions and benefits) and less on that of solidarity (which favours more equal provisions for everybody). In some cases, such as for minimum social pensions in Czechoslovakia, the state will ensure a universal minimum benefit calculated in relation to the absolute poverty line, even to those — such as the long-term unemployed — without social insurance. For some of these benefits, a third component will be made up of compulsory insurance for enterprises where there is continuous exposure to health risk and of additional voluntary private insurance.

While it is hoped that the level of benefits improves, a much greater differentiation in social provisions will thus be unavoidable. Except in the case where basic services and benefits are guaranteed by the state, this may lead to incomplete coverage and social differentiation.

Most central and eastern European governments have announced their intention to continue financing universal child and family benefits from the state budget. Childbirth grants, child-nursing allowance, child allowance, and child-support benefits ought therefore to be maintained broadly intact as a form of general social solidarity. The issue of the child-care allowance, in contrast, is more controversial, particularly in view of the expected rise in the rate of unemployment among women and of the severe budgetary restrictions. In some countries, such as Hungary, the benefit might be retained. This will ensure a minimum income to families with small children; it will also allow for savings on state provision of child-care services (crèches and kindergartens) and unemployment compensation, and lead to lower participation among women in the labour force, as well as lower unemployment of women. This policy approach may, however, prove detrimental in the long term, particularly for children and women from disadvantaged groups.

Arguments are also being put forward for a reduction — or even an outright elimination — of the most important of all family allowances, namely, child allowances, and for the targeting of the resources thus saved on the poor. However, child and family allowances in central and eastern Europe represent around 15-25 per cent of average one-earner household income (as opposed to a 1985 average of 7.5% in OECD countries), which is largely due to the low level of wages of which under the socialist system family allowances were an integral part. For instance, the average benefit per child/year amounts to close to $100 in current prices in Poland, as opposed to an (1984) OECD average of $590, in 1980 prices (Varley, 1986). If their suppression or reduction has to take place, wages ought to increase by a broadly commensurate amount.

Safety nets

While the reform of overall social security and service provisions are likely to take at least 3-4 years before being decided upon and effectively implemented, all central and eastern European countries have already introduced a series of measures, broadly referred to as 'safety nets', to prevent a massive impoverishment of the population during the difficult period of transition to the market economy.

The concept of safety net revolves around that of *absolute poverty line*, which is defined as the income allowing for the least-costly satisfaction of human basic needs for food, clothing, heating, etc. Safety nets aim at ensuring a *minimum family income* (adjusted by family size and structure) by setting minimum levels for wages, pensions and unemployment benefits. In most countries of the region, these minimum provisions are anchored to average wages. In Poland, for instance, the minimum wage corresponds to 35 per cent of the average, while unemployment benefits cannot be lower than 95 per cent of the minimum wage. Minimum pensions are also linked to the average wage. For most families minimum incomes are integrated by child allowances. Not everybody, however, is reached by these minimum provisions. The families of farmers, self-employed workers, and unemployed workers are no longer eligible or do not qualify for unemployment benefits. For these families social assistance, which is mostly funded centrally but managed at the county level, represents the last line of defence against poverty by providing a means-tested benefit to fill the gap between their income and the absolute poverty line.

In addition, as the calculation of minimum family income includes, in most cases, a very limited expenditure on rent, energy, and other items which are increasing in price much faster than the average rate of inflation, social assistance is meant to provide an *ad hoc* means-tested benefit for housing, fuel, the purchase of school books or other special needs, whenever such expenditure exceeds a certain share (10-20%) of household expenditure. Finally, religious and charitable organisations have been encouraged to set up private assistance networks.

In extreme cases, as in the presence of hyperinflation and — if sometimes temporarily — severe shortages, rationing schemes for essential goods were established (as in Bulgaria, Romania and the Soviet Union), while soup-kitchens and overnight shelters for the homeless were opened (as in Poland and Hungary).

III. The Social Impact of the Economic and Social Reforms Underway

While it is everybody's hope that present economic and political reforms will lead to marked rises in income and standards of living in central and

eastern European countries, the economic reforms are, in the immediate, having a negative impact on the well-being of part of the population and, in particular, of those living near or below the absolute poverty line prior to the reform. There are several factors responsible for this decline in well-being:

1. The drop in real household income and savings

Such losses are the result of the rise in uncompensated or partially compensated unemployment and the erosion of real wages, pensions and benefits caused by the removal of subsidies, price liberalisation and large devaluations. In Poland, for instance, average wages, in 1990, declined by 27 per cent (Table 8.2), while involuntary unemployment — unknown prior to the reform — exceeded, at the end of the same year, 8 per cent of the labour force, while the real value of savings fell four-fold. While shortages, typical of the socialist years, have all but disappeared, real consumption of food and other items has declined, though much less than income and savings. In the early phases of the reform, hoarding and supply disruptions may have contributed to the decline in consumption.

The real income of private farmers and members of agricultural cooperatives (a large proportion of rural population in Poland, Hungary and to a lesser extent Bulgaria) ought to have increased, owing to the favourable shifts in the internal terms of trade of agriculture. However, the withdrawal of input-subsidies, the increased competition resulting from trade liberalisation, the increase in trade margins of domestic monopolistic retailers and, most of all, the collapse of domestic demand may, in some cases, have eroded such gains.

The average decline in real household income recorded in all countries of the region in 1990, with the exception of Czechoslovakia, is of an unprecedented magnitude in post-World War II Europe and is uncommon even in developing countries. Widespread and acute forms of deprivation have so far been avoided for four reasons. First of all, such large average drops occur from relatively high levels of income (which can allow for large reductions in consumption without jeopardizing basic needs). Second, such retrenchments have been distributed more broadly than they would have been in most western and developing countries, because of the more egalitarian income distribution structure inherited from the previous regime (Aktinson and Micklewright, 1991). Third, the economic reforms have allowed informal sector and self-provisioning activities which were previously suppressed and are only partially recorded in national accounts. And finally, safety nets, though inadequate, have, in part, reduced the social costs of these reforms.

2. The erosion of social benefits and income transfer to the families

The extent of the family income decline illustrated above is cause for concern for those social groups already near the poverty line under the previous regime, or particularly affected by the reforms underway. Among the first group there is a sizeable proportion of pensioners, large families, single-parent families, people with handicaps, minority groups and alcoholic or broken families. Among the second group are youth in search of first employment, the long-term unemployed, and low-skilled workers in sectors being retrenched such as heavy industry.

Prior to the reforms, the poor were estimated to account for some 14 per cent of the population in Hungary, between 20-25 per cent in Poland and Yugoslavia, between 18-32 per cent in the Soviet Union (depending on whether the poverty line of 75 roubles in 1985 or 100 roubles in 1989 was chosen).

For most of these people, the main, and in some case the only, source of income was social transfers. Most retirees depend exclusively on public pensions, while, as noted in Section I, social security transfers accounted, prior to the crisis, for between one-third and one-half of the disposable income of single-parent or large families, or of other groups at risk.

Despite this and despite the generalised drop in earnings, the real value of social transfer has been eroded significantly for *all* social groups. In Bulgaria, total real social transfers declined by 37 per cent in 1990 (Table 5.4 and *IMF Survey*, 18 March 1991). In the same year, in Poland, the decline was 11 per cent (Tables 8.2 and 8.3). In addition, about 5 per cent of the 1990 total Polish social transfer (accounting for about 0.5% of NMP) was diverted to unemployment compensation and expanded social assistance. While not enough to tackle the significant rise in poverty and unemployment that year, this reallocation of social transfer contributed to squeezing still further the real value of pensions and family allowances. Even in Czechoslovakia, the country with more favourable initial conditions and which followed a more gradual approach, social transfers declined in 1990 by 6 per cent and are projected to stagnate in 1991 (Tables 6.8 and 6.9). In 1991, furthermore, about 11 per cent of total social transfers will be used for unemployment and price increase compensation, thus compressing by a commensurate amount the real value of pensions and family benefits.

The erosion of the real value of social transfers has therefore accentuated the decline of other sources of household income. Its indiscriminate nature furthermore has been regressive from an income distribution perspective (see Table 7.4). Social policy has thus been pro-cyclical and has largely failed the objective of offsetting the decline in household income.

3. The decline in real government expenditure on health, education and child care

While one of the immediate objectives of the reform of social policy was to improve the quality of public services, particularly health service, the drastic reduction in real government expenditure as part of the stabilisation programme has not completely spared public expenditure on social services. While less affected than other categories, real public expenditure on health is expected to decline in Czechoslovakia in 1991, and government expenditure on education did decrease in Poland in 1990. In most countries, furthermore, state expenditure on child-care services declined dramatically with their decentralisation to underfinanced local authorities. In a number of cases, this decline has meant lower real wages for public employees such as teachers, doctors nurses, etc., thus leaving the amount, if not the quality, of such services unaffected. There have been cases, however, where personnel have been made redundant and public facilities closed. This contraction in the supply of public services has at times been heightened by a contraction in demand following the introduction of substantial user-fees and cost-sharing arrangements for kindergartens, school supplies, drugs, etc. The effectiveness of such services was also affected by the scarcity and high domestic cost of foreign exchange which made the shortage of imported inputs even more acute than before.

For all these reasons, there are already signs of a decline in service utilisation. This has been most obvious so far for child-care services, complementary school services (such as after-school tutoring, summer camps, etc.) and social amenities (such as public libraries).

4. Relative price effect

In addition to the decline in consumption caused by the fall of real income, the welfare of children and other marginal groups has been (and is being) affected also by the increase in the *relative* prices of basic goods and services. Under the socialist regimes, the prices of most basic goods (including food, drugs, housing, energy, and transport) were kept low through public subsidies, while those of non-basic goods were high because of the substantial turnover tax to which they were subjected. The relative price of, say, food versus that of a car was much lower than in market economies. The removal of subsidies and trade liberalisation tend to exert opposite influences on the relative price structure by increasing the relative price of 'basic' against 'non-basic' goods. Despite its low price-elasticity, the demand for basic goods will probably contract more than would be expected given the decline in income.

5. Overall income distribution effect

Unless specific redistributive measures are introduced over the medium term, the increase in the number of those living below an absolute poverty line might be exacerbated by the polarisation in income distribution resulting from the growing differentiation in wages, salaries and other income. Indeed, as a result of the reforms underway, the income distribution pattern of the countries of central and eastern Europe is likely to become similar to that prevailing in the western economies. This assumes that they will adopt redistributive policies similar to those followed in the latter countries approximated (very tentatively) by the ratio of social transfers to GDP (last column Table 4.4). If this is not the case, income inequality is more likely to be pronounced and similar to that typical of most middle-income developing countries.

The potential poverty-inducing effects of the expected shift in the pattern of income distribution is illustrated in stylized form in Figure 4.1 which depicts graphically the hypothetical changes in the incidence of poverty resulting from the economic reforms underway. The distribution of disposable income among households prior to the introduction of the reforms is identified by the curve ID_0, whose shape is indicative of the relatively little inequality prevailing in socialist countries. As indicated by the data of Table 4.5, in such countries the income of the top 20 per cent of the population was about three times as large as that of the bottom 20 per cent. Average household income was AHI_0. Given an absolute poverty line, there were P_0 per cent of households in poverty.

In the initial phase of the reform, excessive polarisation is being contained by anti-inflationary stabilisation policies imposing heavy taxes on wage increases (mostly in the still predominant public sector) and by the introduction of minimum wages and pensions as part of the safety nets. For these reasons the decline in average income occurring during the initial phase of the reform is not likely to be accompanied by fundamental changes in the pattern of income distribution. In Figure 4.1, therefore, household disposable income immediately after the economic reform shifts downward by the same amount (say 10%). Average (disposable) household income declines therefore by 10 per cent from AHI_0 to AHI_1, while the number of households in poverty increases from P_0 to P_1 per cent, because of the downward shift in the income distribution curve from ID_0 to ID_1.

Figure 4.1 - Household Income Distribution and the Incidence of Poverty

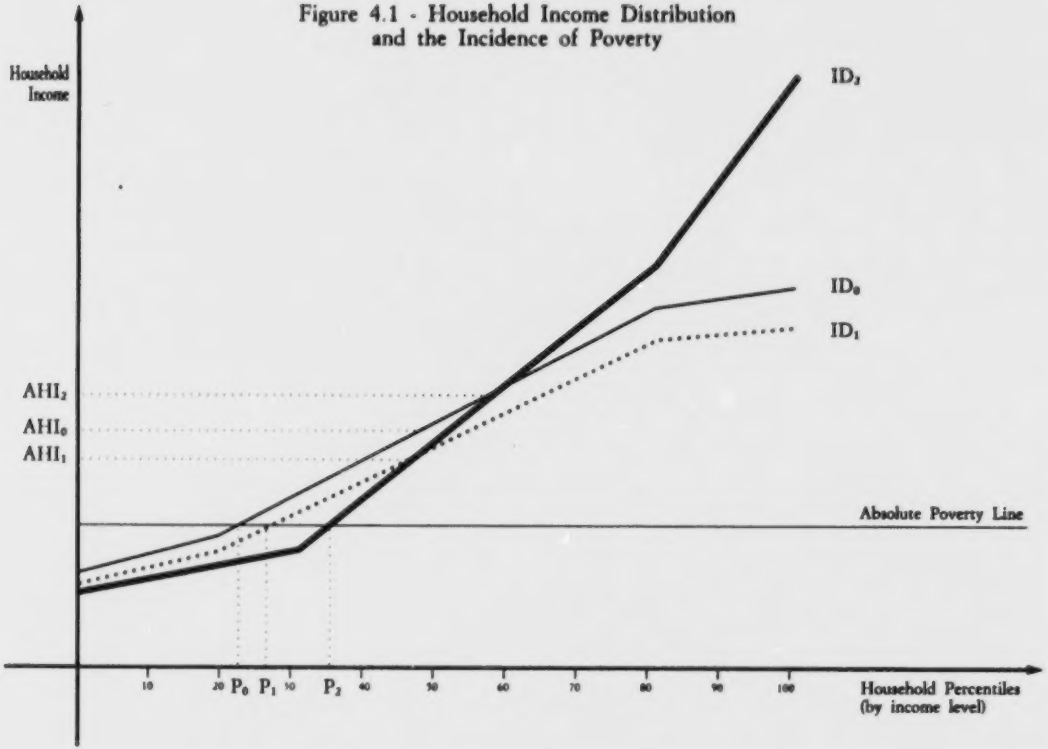

TABLE 4.4 *Income distribution patterns in industrialised and middle-income developing countries in mid-1980s*

	GDP/c [1]	Highest quintile of households	Lowest quintile of households	Ratio	Social transfer [4]/ GDP ratio
		A. *Centrally planned economies*			
Czechoslovakia	—	—	—	2.4 [2]	14.7 [2,3]
Hungary	2460	32.4	10.9	3.0	—
Soviet Union	—	—	—	3.4 [2,3]	—
Poland	1860	35.2	9.7	3.6	9.6 [6,3]
Yugoslavia	2520	42.8	6.1	7.0	—
		B. *Low-moderate inequality market economies*			
Sweden	19300	30.9	11.1	2.8	19.3 [3]
Japan	21020	38.6	8.0	4.8	12.0 [3]
F.R. Germany	18480	38.7	6.8	5.2	15.1 [3]
Netherlands	14520	38.3	6.9	5.6	—
		C. *Relatively high inequality market economies*			
Italy	13330	42.2	6.9	6.1	17.9 [3]
United Kingdom	12810	42.0	6.1	6.9	11.2 [3]
France	16090	43.0	5.9	7.3	20.3 [3]
United States	19840	41.9	4.7	8.9	9.6 [3]
Australia	12340	42.2	4.4	9.6	9.7 [3,5]
		D. *Middle-income developing countries*			
Costa Rica	1690	54.5	3.3	16.5	—
Venezuela	3250	50.6	4.7	10.1	—
Malaysia	1940	51.2	4.6	11.1	—
Brazil	2160	62.6	2.4	26.1	—

Source: GDP/c data: World Bank (1990); income distribution data: for Hungary, Poland, Yugoslavia, Australia and panel D: World Bank (1990); for Czechoslovakia, panels B and C and data on social transfers/GDP ratio: Boltho (1991); for the USSR: Braithwaite and Heleniak (1989).
Note: [1] GDP per capita (in 1988); [2] ratio of top to bottom decile; [3] late 1980s; [4] social security benefits and social assistance grants; [5] Gordon (1988); [6] see Chapter 6; [7] see Chapter 8.

In the second phase of the economic reform, GDP, average household income and income inequality are expected to grow in parallel. Even assuming that a strong recovery will push up average household income by 30 per cent to AHI_2 (in, say, 3-4 years) and that the income distribution will approach the shape (ID_2) of low to moderate inequality market economies, such as Germany and the Netherlands (where the income of the top two deciles is about five-six times bigger than the bottom two

deciles; Table 4.4, panel B), poverty would actually increase to P_2, as illustrated in Figure 4.1. Obviously, the effect of poverty would be much greater if income-distribution patterns such as those prevailing in moderate-to-high inequality market economies such as the United States, Australia or most Latin American countries were to be adopted. While the above discussion is of a purely illustrative nature, a broad conclusion is clear: even in the presence of rapid growth starting, say, in 1992 or 1993, the substantial shift in the distribution of household income expected to follow on from the reforms will not reduce poverty for several years. Indeed, poverty may well increase in the short to medium term.

Limiting the spread or persistence of poverty might require therefore *additional* efforts in the field of labour market and income policies and in that of redistributive and targeting policies. While income policies aimed at reducing the growth of wages and of their spread will be difficult to implement over the medium term, there might be more room for redistributive and active labour market policies (focusing on retraining, labour mobility, promotion of self-employment through credit and technical assistance and, in extreme cases, public work schemes). The latter are generally accepted in principle, but their application on a scale adequate to meet real needs is made difficult by the possible further decline in government revenue (relative to GDP) following privatisation, likely informalisation of the economy, and from the unavoidably slow and gradual application of the new tax reform. The targeting of resources on the truly needy is at the heart of the safety-net concept, particularly its social assistance component. Its limitations and options for improvements are examined in the next section.

6. Limitations of the present approaches to safety nets

In the initial phase of the reform, the well-being of children and other vulnerable groups has not been adequately protected, in most cases, due to the delayed introduction and limited extent of safety nets. Five factors may have led to this situation. To start with, minimum wages, unemployment benefits and pensions, around which existing safety nets are built, are very low. In Poland, for instance, minimum salaries are equivalent to about $40 a month, while domestic prices for most goods tend to approach international prices. In many cases, this is too low and barely allows for the satisfaction of basic food, clothing and local transport needs. In addition, the calculation of the poverty line does not adequately reflect the increase in rents and other housing costs which are escalating rapidly.

Second, the funds destined for unemployment compensation and social assistance, in the majority of cases, have not matched the growth in

the number of jobless and the spread of poverty. In Poland, for instance, allocations for these two sectors in 1990 were made on the assumption that unemployment would not exceed 400,000 units by the end of the year. At the end of 1990, however, this number had become three times as great. Furthermore, social assistance benefits are provided by local authorities and charitable organisations and vary considerably with the self-financing capacity of the various counties, municipalities and private organisations. Social assistance coverage and generosity are therefore incomplete and uneven.

Third, although desirable in principle, targeting a part of social transfers on the poor by means of unemployment and means-tested social assistance benefits gives rise, in practice, to a number of problems. The reduction in the real value of pensions and family allowances which it implies would expose an important part of the population, in a period of declining real income, to the risk of poverty and thus require additional social assistance payments. With increased competition among various types of social transfers, both safety nets and traditional social transfers are underfunded. Fourth, the administration of means-tested social assistance benefits on a major scale involves substantial costs in their administration. In addition, like all means-tested benefits, social-assistance grants have been shown to cause low uptake rates because of the social stigma it involves (particularly in countries with no tradition of applying for aid), while engendering well-known work disincentives.

Finally, the existing monetarisation of social assistance, as well as of other benefits, does not provide adequate protection during a period of hyperinflation, as there are limits to the extent and frequency of indexation.

IV. In pursuit of adequate safety nets for children and other vulnerable groups

The previous analysis has essentially tried to highlight two points. First, the implementation of economic reforms is encountering a number of difficulties which might prolong the period of transition, and delay the economic recovery and the improvement in the standard of living. These difficulties arise from problems in the design and sequencing of the reforms, and from the pace of their implementation, as well as from external factors. Among these, the prolonged uncertainty, terms of trade shocks and disruptions in oil supplies caused by the Gulf war; the moderate recession underway in most OECD countries; and the limited flow (so far) of direct foreign investment. As suggested by the experience of the erstwhile German Democratic Republic, these problems may lead to a near-collapse of the former economic structures and to heavy social

costs. Second, with the possible exception of Czechoslovakia, social policy and distributive issues have not received adequate attention during the process of transition to the market economy. While safety nets have been put in place in all countries, their underlying philosophy, broadness and under-funding have reduced their effectiveness. Limited resources, weak institutions, and a fatalistic attitude towards the spread of unemployment and other forms of marginalisation have been unable to prevent a substantial increase in poverty and other forms of social fallout, as indicated in Chapter 1. Children, particularly those from large, single-parent or crisis families, from ethnic minorities or areas particularly affected by economic restructuring, as well as youth in search of first employment, are among those most affected.

It is everybody's hope that, despite the initial obstacles encountered, the economic reforms will continue. Without them, the countries of eastern and central Europe would be doomed. However, a more realistic, better sequenced and possibly a more phased approach is required. In addition, much more vigorous policy action is needed in the field of distributive issues, social policy and safety nets. Without it, it will be difficult to avoid a substantial impoverishment of large sections of society, a mass migration towards the western countries and a retrogression in the well-being of children and other vulnerable groups.

Under conditions of greater stability and affluence than those currently prevailing in the region, social policy could aim, simultaneously, at ensuring minimum living conditions, as well as at avoiding excessive polarisation in the distribution of income and in the economic distance among households. In view of the many and complex changes induced by the political and economic changes underway, however, social policy, safety nets and redistribution might aim more realistically at achieving the goal of ensuring at least minimum (but adequate) living conditions for all. Such an approach requires specific provisions in the following four areas: income maintenance, indexation, direct provision of goods and services, and monitoring of social conditions.

1. Income maintenance

In order to ensure a minimum (though adequate) monetary income to all families, adjusted by size and structure, the following measures would need to be implemented:

— Increasing existing minimum wages, pensions and unemployment benefits to more realistic levels and in line with the changes intervened in absolute and relative prices. As noted in several case studies, the food share in total family consumption reaches or exceeds the 50 or 60 per cent

benchmark in many family categories. Such a high level of food share is observed only amongst the poor in developing countries and suggests insufficient income and possible deprivations in areas other than nutrition. In the European Community, for instance, the poverty threshold is computed using a food share (allowing for a minimum basket of commodities ensuring basic nutritional requirements) varying between 30 to 40 per cent of household income (Teekens and Zaidi, 1990).

— Ensuring more active labour market policies. This would entail greater efforts on retraining and on ensuring labour mobility from industries in decline to new ones, as well as credit, technical assistance and institutional support for the establishment of micro-enterprises. Specific measures will be required, in particular, for youth in search of first-time employment, for the unskilled and the long-term unemployed. Under present conditions, such categories have to rely on means-tested social assistance benefits. A preferable alternative would include public works and apprenticeship programmes remunerated at around the minimum-wage level, as widely followed in countries such as Sweden, Italy, Chile and other developing countries.

— Retaining universal child and family benefits and extending them to children of parents who are unemployed or not part of the labour force. Correcting this bias, inherited from the socialist policies, becomes even more compelling in a period of growing unemployment. In addition, child allowances could be improved upon by graduating them according to the age of the child. The proposal to cancel or sharply reduce them in order to focus resources on the 'truly needy' should therefore be rejected. However, to avoid transferring resources to the well-off section of society, family benefits should be included among the assessable incomes subject to the new income tax. Moreover, to avoid diversion to unintended use, part of these benefits could be issued in the form of vouchers (such as food-stamps, for instance) valid for the purchase of goods for children, to be redeemed in private or public stores.

The present trend, as observed in Hungary, for instance, to encourage child-care leave (with a partial allowance) up to the age of three years might also be supported. Particularly in a period of growing unemployment and declining funds for crèches, this would ensure a minimum income for the caring parent and budgetary savings on unemployment payments and expenditure on public services. The risk of this approach is that it will inevitably reduce the participation of women in the labour force and strengthen the gender duality of labour policies.

— Social assistance would retain an important, though less central role in income maintenance by providing targeted transfers to those not reached by the provisions just described. The effectiveness of targeting would be greatly enhanced from the distributive and administrative

perspective if it were carried out according to some objective criteria such as geography (the poorest regions) or easily identifiable population groups (pregnant women or small children). As substantial empirical evidence suggests, targeting by means-testing and other discretionary methods involving the earmarking of individuals should be avoided to the extent possible because of its cost and stigmatising effect.

2. Indexation

While all countries have introduced some mechanisms to compensate for price increases, indexation suffers at present from the following inadequacies: it is not automatic; it is carried out every quarter or even less frequently and on an *ex post* basis; and it does not differentiate the extent of indexation by level of wages and benefits. As a result, household income has been excessively eroded, thus making *ad hoc* additional payments necessary. Moreover, the decline in the income of the poor and near-poor has been of the same proportion as that of the better-off.

A more appropriate indexation would require automatic adjustments carried out periodically and *ex-ante* on the basis of the average rate of inflation projected over the period chosen. In addition, and central to the objective of combatting poverty, the indexation of minimum income should compensate fully for the price increases. In Bulgaria, for instance, minimum wages were increased in early 1991 in line with the increased cost of a minimum subsistence basket of goods and services, while the indexation of other wages was only 60 per cent (*IMF Survey*, 18 March 1991). Family benefits for groups at risk, such as large or single-parent families, or pensioners on minimum benefits, should also be fully indexed.

3. Direct provision

Free access to health, education and kindergarten services ought to be retained in all countries. Nominal fees which would account for 5-10 per cent of the actual cost of services and complementary inputs (such as school books and drugs) could be introduced or generalised to increase efficiency. Substantial fees for basic services (such as school books in compulsory education, essential health services for children) should be avoided as, in most industrialised countries, health, education and child-care services are generally considered 'public goods' financed through taxation or compulsory insurance.

At least during the initial years of the transition to the market economy, public policy may also have to include measures for the free provision of school meals (including kindergartens) and social-purpose housing. Milk for children and school feeding are a highly efficient

method to ensure nutritional standards and child growth. They also represent a simple way to target resources to an especially vulnerable group (IMF, *et al.*, 1990). The risk of leakage to better-off groups is limited (as children of well-off families may not make use of these services), while their cost is relatively modest. As shown in Tables 6.1 and 6.3, school meals benefitting 85 per cent of all children in kindergarten and compulsory school absorbed, in 1988, in Czechoslovakia, a mere 0.4 per cent of GMP.

Measures are even more necessary in the housing sector, where the shortage inherited from the previous regime combine with the current withdrawal of housing subsidies and moves towards privatisation to produce unprecedented increases in rentals. To avoid a further spread of homelessness, a gradual and controlled liberalisation of the housing market might be necessary, while measures are needed, in particular, for safeguarding the rights of low-income groups, particularly large families, pensioners and health-impaired persons to remain in the flats or houses they currently occupy at rent-controlled prices. Means-tested social assistance benefits for housing costs and utilities are also required (and have gradually been instituted). In addition, social-purpose housing for the poor not covered by the above provisions could be organised by requisitioning and renovating — with the help of private organisations — (through public work schemes or by the beneficiaries, for instance — abandoned public buildings, or vacated barracks.

Finally, public provision may ensure that critical drugs and other key imports for children and other vulnerable groups are secured through the priority allocation of foreign exchange.

4. Monitoring child welfare during the transition

The prior discussion suggests that the development of a new social policy and broad safety nets is still in its initial phase. The situation varies substantially from country to country and with the overall pace of economic reforms. Because of the immensity and urgency of the task ahead, new policies are being implemented with only limited knowledge of their likely effectiveness and of their impact in market economies, while corrections may be needed even shortly after their introduction. In addition, the social impact of the social and economic reforms underway is almost exclusively assessed in terms of unemployment and changes in the prices of some essential commodities.

An adequate safety net would require setting up an appropriate mechanism to monitor the development of social policy and to assess the comparative efficiency of alternative social policies. Even more impor-

tant, simple and timely mechanisms are required to monitor changes in the well-being of children and other vulnerable groups during the transition to the market economy. It would be useful to include in such a monitoring system not only information on income, prices, benefits, and demographic characteristics of the population (which are already produced or obtainable from the existing household expenditure surveys), but also data on effective access to health, child care, education and housing, as well as changes in health status, nutrition and homelessness.

A simple 'early warning' system which included part of this data ought to collect and analyze periodically (at least twice, and possibly four times, a year) information on the social situation. The result — a simple 'social monitoring report' — should be submitted regularly to the government and to the public at large.

5. The resource dimension

The above measures will certainly entail a sizeable cost for the budgets of central and local governments. However, the measures are broadly consistent with the objectives to achieve fiscal balance, reduce the role of the government in the economy and shift the savings made on producer and consumer subsidies and other sectors towards investment.

This approach would require leaving broadly unchanged real expenditures on health, education, child care and social transfer to a pre-crisis level, while improving their efficiency and distribution. This however may not be an easy objective to achieve whenever the elimination of consumer and producer subsidies is accompanied by the need to do away with huge budget deficits because of the overall decline in GDP that such policy entails. This was the case of Poland in 1989 (when the deficits equalled 13% of GDP) and is currently that of the Soviet Union. In all these cases, the adjustment policy should aim at maintaining constant the share of social expenditure on GDP.

In addition, the approach to safety nets illustrated above would require an additional 1.5-2 points of GDP for unemployment compensation, active labour market programmes and strengthened social assistance (see Table 2.6). This represents an important, but achievable, increase when compared to the 0.5 per cent allocated by Poland in 1990 (Table 8.3) or to the 1.1 per cent foreseen in Czechoslovakia in 1991 (Tables 6.8 and 6.9). This additional expenditure can be more than compensated by the savings from the withdrawal of producer and consumer subsidies (which are only partially compensated for) and military expenditure cuts and by the debt-relief measures announced which ought to reduce substantially the domestic currency burden of the servicing of the interna-

tional debt. In Czechoslovakia, for instance, the 'savings' on subsidies and defence in the 1991 budget account for 10.5 per cent of GMP.

The objective of redistributing benefits through the government budget requires not only giving priority to social expenditure in the allocation of government funds, but also the expeditious implementation of a long-awaited tax reform of which the enlargement of the tax base and the introduction of local-level taxation would be essential components. From this perspective, a policy operating exclusively from the expenditure side would not be able to achieve the desired objectives.

Part II

Reforming Social Policies for Children in Central and Eastern Europe: Four Country Case Studies

CHAPTER 5

CHILDREN AND THE TRANSITION TO MARKET ECONOMY IN BULGARIA: 'SHOCK THERAPY' WITH A DIFFERENCE?

Ivan Chernozemski

I. The social security system of past and present

The transition to the market economy and political democracy started in Bulgaria later than in most other countries of central and eastern Europe. Certain measures taken at the end of 1989 and in 1990, during the painful political tug-of-war which lead to democracy, can be seen as the first steps on the road to the market economy. However, the first comprehensive reform package was only put into effect from 1 February 1991. Consequently, the current social security system is still the old one with only limited, though important, changes. Social policy has changed inasmuch as the overall body politic has become more pluralistic, as the implications of the crisis and transition are better understood, and as the direction of future action becomes more clearly defined.

Social policy in Bulgaria, in a historical perspective, should be seen in the context of rapid modernisation and industrialisation of a poor, overwhelmingly agrarian small country in the Balkans. In fact, after World War II, Bulgaria underwent a major transformation from a largely rural to an essentially urban society in which 67 per cent of the population lived in towns in 1989 (BCSO, 1991a, p. 22). This shift is the largest of all western, southern and eastern European countries (see Deacon, 1987). Between 1937 and 1980, the country's relative economic development level improved from the last position but one in Europe (32nd) to 23rd according to composite development indicators (Ehrlich, 1990, Table 8). From a country without public health insurance, Bulgaria achieved full health insurance during this period (see Minev, 1990). Such a great and often enforced transformation naturally involved huge imbalances and suppressed tensions which were not always addressed adequately by social policy.

The political conditions under which the social security system func-

tioned until a year ago were characterized by an exclusive domination of the Communist Party and by a lack of initiative on the part of civil society. Trades unions, in principle the guardians of labour interests in a socialist society, provided only token representation and, in fact, acted as transmission belts for the Party-State. Other institutions having a mandate for particular interests (Fatherland Front, cultural associations, churches, minority organisations, etc.) were subject to the same all prevailing control and therefore could not function adequately. The badly articulated divergence of specific interests was suppressed in the name of a highly manipulated 'social interest' which took no heed of dissenting views. Thus the inherent arbitrary character of decision-making can be seen as the most counter-productive element of the social policy of the Party-State. Arbitrariness and uncontrolled political discretion, however, are only a pretext for bad decisions. However, an objective judgement of past social policies and the social security system should proceed case-by-case and issue-by-issue in order to prevent throwing the baby out with the bath water.

1. Social policy and income distribution

Primary income distribution

In accordance with Marxist doctrines, social equity was pursued in Bulgaria by very stagnant and flat income distribution patterns (see Tables 5.1 and 5.2) which provided a solid backdrop to social policy in the secondary distribution. Both the shares of wages and social security contributions in NMP increased rapidly in the first period. Then, during the 1980s, these shares remained stationary at around one-third and 11 per cent of the national income respectively (or 28% and 8.8% of GDP). Production, income and real wages increased rapidly at first and then more modestly in real value. The ratio of income to production deteriorated in time due to increasingly inefficient use of capital stock. Subsidiary and private activities stagnated in real value and declined in proportion to national income, showing that private (individual) accumulation built up little else than a monetary overhang in Bulgaria.

The stability of the shares of national income in the 1980s was accompanied by an extremely and increasingly compressed wage spread (see Table 5.2). In 1990, two-thirds of all employees in the public sector (state and co-operative with over 95% of total employment) earned around or less than average wages (337 leva). The median wage (290 leva) was very close to the average which was about twice the prevailing minimum wage (165 leva). More than half of the labour force received wages between 200-350 leva and only 3.5 per cent earned less than the minimum wage (part-time jobs).

TABLE 5.1 *The value composition of national product and the distribution of national income 1980-1988 (in millions of current leva, %)*

	1952	1970	1980	1985	1987	1989
National product	4945	26243	57902	65413	69863	90528
National income	2581	10527	20509	22151	23381	30840
Distribution of national income:						
wages and salaries	27.7	40.9	35.7	34.4	34.	37.5
auxiliary & private	23.9	8.3	8.9	9.4	8.8	8.5
turnover taxation	24.9	17.6	21.2	17.0	18.	14.8
profit/loss	9.1	20.4	22.2	27.8	25.2	27.5
social security cont.	2.4	5.4	11.2	11.2	11.1	11.5
other	12.0	7.4	0.4	0.2	2.9	0.2
Memorandum items:						
GDP (at current prices)	N.A.	N.A.	25791	32595	36531	39579
CPI (retail prices)	N.A.	N.A.	100	114.9	121.2	131.7
Real wages index	36.4	84.2	100	111.0	117.0	124.4
Social security contr. ind.	2.7	24.5	100	107.9	113.3	154.5
National income/product	52.2	40.1	35.9	33.9	33.5	34.0

Source: Own calculations based on data from the Central Statistical Office, BCSO (1990, pp. 50, 115; 1991, p. 47).

TABLE 5.2 *Distribution of monthly wages according to wage brackets, July 1990 (in current leva and in %)*

Monthly Wage	Total	Workers	Others
< 165	3.5	4.3	1.4
166-180	6.5	8.1	2.7
181-200	11.7	14.3	5.3
200-220	17.5	21.1	8.8
221-240	24.1	28.4	13.8
241-260	31.1	35.9	19.7
261-280	38.7	43.3	27.7
281-300	47.3	51.5	37.6
301-350	63.9	65.7	59.7
351-400	76.2	76.8	75.1
401-450	84.5	84.5	84.9
451-500	89.8	89.9	90.4
501-600	95.4	95.2	96.2
601-700	97.8	97.6	98.4
701 >	100.0	100.0	100.0
Memorandum items:			
No. of employees ('000)	3064	2162	902
Average wage (leva)	337	331	352

Source: BCSO (1990, pp. 120-1; BCSO, 1991b).
Note: The sample covers 78.3 per cent of public (state & co-operative) employees, private sector and self-employed excluded.

The wage spread between sectors and professions has exhibited an even more uncompromising (and irrational) pursuit of equity. The largest difference in wages was 21 per cent between those in construction (the highest paid workers after the very small scientific group) and health, finance and social security (the lowest paid but rather educated) sectors. The inter-sectoral differentials between the best and worst paid workers narrowed from 1.87 in 1948 to 1.67 in 1970, to 1.45 in 1985 and to 1.21 finally in 1989 (BCSO, 1990, p. 116). Education has been penalized by the sectoral wage distribution which is reinforced by the intra-sectoral wage distribution. Specialists and managers earn 11 per cent and 50 per cent more than workers respectively. It should be mentioned, however, that, in a shortage economy, wage differentials do not always tell the true story about the welfare of particular social groups. People in the *nomenklatura* or in priority sectors (like large companies in heavy industry) had access to a number of privileges (e.g., housing) which were unavailable to others.

There were three major consequences of this compressed wage distribution, besides the obvious implications of the disincentives to education and achievements in general:

a) relatively few transparent inequalities to be corrected by secondary income distribution and social policy;

b) the overwhelming majority of the Bulgarian population is extremely vulnerable to the present economic crisis as their wages are very low;

c) few incentives in the system (which adversely affected the overall efficiency of the economy).

Secondary income distribution: transfers and subsidies

Wages, the main source of income, accounted for an average of 54 per cent of total per capita household income in cash during the 1980s. Non-wage income from economic activities in the public sector, interests, loans and insurance made up a relatively small and stagnant 13 per cent as did private auxiliary activities (12%), whereas the share of social security benefits increased almost continuously from 8.7 per cent in 1965 to 18.7 per cent in 1989 (see Table 5.3).

Income in kind, on the other hand, declined from 47.3 per cent of the total nominal income of the population in 1952 to 14.6 per cent in 1989. The increasing share of social security transfers in household income (not including consumer subsidies and income in kind) has been accompanied by a slow-down in the increase (and eventual decline in 1990 and 1991) in the overall consumption of the population (BCSO, 1990, p. 98). Despite the monetary overhang which is due to persistent shortages on consumer markets, the savings ratio declined dramatically from 10.6 per cent in

TABLE 5.3 *Distribution of household income according to the source of income 1965-1989 (%)*

	1965	1970	1975	1980	1985	1987	1989
Wages & salaries	58.3	54.8	56.0	57.9	53.7	53.9	49.4
Contracts in public sec.	—	—	—	0.4	0.4	0.4	0.5
Auxiliary & private	15.8	13.9	11.7	10.5	12.7	11.1	13.0
Cash transfers	8.7	11.6	12.2	16.4	17.3	18.4	18.7
Income from deposits	5.9	7.7	9.5	8.4	9.4	8.9	9.8
Loans	3.8	4.6	3.1	1.9	1.7	2.0	1.9
Others	7.5	7.4	7.5	4.5	4.8	5.2	6.7
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Memorandum items:							
Average per capita household income (current leva)	691	1069	1446	1864	2238	2481	2935
Nominal income of the population (million current leva)	2689 *	8984	—	18077	23167	25769	28713
Of which:							
In cash (%)	52.7 *	84.3	—	83.4	83.6	83.8	85.4
In kind (%)	47.3 *	15.7	—	16.6	16.4	16.2	14.6

Source: Central Statistical Office (1991); BCSO (1990, p. 125).
Note: * Data from 1952.

1985 to 3.2 per cent in 1989 and kept on declining in 1990 — clear evidence that economic decline had started to affect real income.

Besides direct transfers in cash and kind to the population, indirect transfers such as subsidies and other expenditure by the state budget have played an important role in public welfare and secondary distribution (see Table 5.4).

As economic problems intensified during the 1980s, budgetary redistribution increased from 51 per cent of GDP in 1980 to 65 per cent in 1989. Preliminary data about 1990 suggest that the extent of redistribution kept on increasing as the GDP fell by about 11 per cent (see Robinson, 1991, p. 12). In real terms (at 1980 prices), subsidies increased by 64 per cent between 1980 and 1988. They fell by 10 per cent in 1989 and by more than 20 per cent in 1990 according to preliminary indicators. Social security expenditure increased by 53 per cent in real terms between 1980 and 1989 and declined by 18 per cent in 1990. Further contraction of production (and consequently reduced tax revenues) are expected with three-digit inflation in 1991. Due to these factors, budgetary redistribution of GDP may increase even if subsidies are cut substantially and other items of expenditure stagnate (the planned social expenditure figure for 1991 shows substantial growth in real terms if inflation remains under 500%).

Families with children have exhibited a high dependency on social

TABLE 5.4 *Government expenditure by main categories as share of total expenditure and of total GDP 1980-91 (in millions of current leva and in %)*

	1975	1980	1985	1988	1989	1990	1991 [1]
	Consolidated					Planned	
	(A) *Share of expenditure*						
Total expenditure	100	100	100	100	100	100	100
Current expenditure	88.9	90.5	86.4	91.1	91.1	94.2	96.4
wages & salaries	7.9	8.4	7.5	7.1	7.0	8.5	9.2
maintenance & oper.	27.6	28.3	27.3	22.3	23.5	23.9	19.3
defence	8.4	8.6	8.2	8.3	8.0	8.2	8.6
subsidies	30.1	22.9	20.0	26.6	24.1	22.9	5.8
external debt & other	3.6	5.7	13.0	6.8	8.0	10.5	16.5
internal debt & other	—	—	—	—	—	0.8	6.8
social security	12.3	18.7	20.4	18.8	20.5	20.2	30.2
pensions	7.5	11.7	11.9	11.6	11.9	12.5	18.3
benefits & assis.	4.8	6.9	8.4	7.2	8.5	7.8	11.9
Capital exp.-investment	11.1	9.5	13.6	8.9	8.9	5.8	3.5
Surplus/deficit (—)	1.0	0.7	0.6	0.4	0.5	—3.9	—10.7
	(B) *Share of GDP*						
Total expenditure	—	51.3	57.3	60.5	62.0	64.7	—
Current expenditure	—	46.5	49.4	55.2	56.5	61.0	—
wages & salaries	—	4.3	4.3	4.3	4.3	5.5	—
maintenance & oper.	—	14.5	15.6	13.8	14.6	15.5	—
defence	—	4.4	4.7	5.0	4.9	5.3	—
subsidies	—	11.7	11.4	16.1	15.0	14.8	—
external debt & other	—	2.9	1.7	4.1	5.0	6.8	—
internal debt & other	—	—	—	—	—	0.5	—
social security	—	9.6	11.7	11.4	12.7	13.1	—
pensions	—	6.0	6.9	7.0	7.4	8.1	—
benefits & assis.	—	3.6	4.8	4.4	5.3	5.0	—
Capital exp.-investment	—	4.8	7.9	5.3	5.5	3.7	—
Surplus/deficit (—)	—	0.3	0.3	0.2	0.3	—2.5	—
Memorandum items (1) [1]:							
Education	—	4.6	4.5	4.5	4.6	5.4	—
Culture	—	1.1	1.0	1.0	1.0	1.1	—
Health	—	3.0	3.0	3.0	3.1	3.8	—
Sport & recreation	—	0.1	0.4	0.4	0.5	0.3	—
Memorandum items (2):							
Total expenditure	9223	13221	18666	23219	24378	25875	70477
GDP (mn. current leva)	—	25791	32595	38345	39579	45088 [2]	—

Source: Ministry of Finance (1991); Darzhaven Vestnik (1991, p. 2).
Notes: [1] The budget for 1991 is tentative and subject to change. [2] Memorandum items (1) for 1990 are based on preliminary actual figures and not on plans.

transfers and therefore are rather vulnerable to any decrease in the real value of these transfers (see Table 5.5). On the other hand, the overall dependency ratio of households was usually somewhat higher than that of the small families with one or two children due to the high and increasing

TABLE 5.5 *Distribution of per capita household income according to source of income and family size 1975, 1980, 1989 (%)*

	Single persons	Couples with					Total
		0	1	2	3	4>	
		children					
1975:							
Wages & salaries	35.8	57.2	66.8	68.6	65.1	64.0	64.1
Social security	31.9	18.0	10.2	11.6	16.8	15.1	13.9
Auxiliary & private	15.5	16.9	11.0	11.0	14.9	12.9	13.4
Othe	16.8	7.8	9.0	8.8	8.2	8.0	8.6
1980:							
Wages & salaries	36.1	58.6	73.9	69.6	63.0	56.3	65.0
Social security	40.8	21.9	12.9	15.9	20.6	23.3	18.3
pensions	40.2	20.7	6.8	5.7	3.6	4.6	13.3
child benefits	0.1	—	3.3	7.1	13.1	15.4	2.9
social assistance	0.5	1.2	2.8	3.1	3.9	3.8	2.1
Auxiliary & private	13.8	15.2	8.2	8.9	9.5	11.3	11.7
Other	9.3	4.3	5.0	5.6	6.9	8.6	5.0
1989:							
Wages & salaries	31.7	39.2	73.6	68.2	58.6*	—	56.5
Social security	39.3	34.4	9.8	13.4	19.7*	—	21.2
pensions	38.5	33.3	3.7	2.0	1.7*	—	16.6
child benefits	0.1	0.1	2.6	7.7	14.4*	—	2.3
social assistance	0.7	1.0	3.5	3.7	3.6*	—	2.3
Auxiliary & private	18.4	22.7	5.5	6.1	6.9*	—	14.7
Other	10.6	4.5	11.1	12.3	14.8*	—	7.6

Source: Household surveys 1975-1989, Central Statistical Office.
Note: * 3 or more children.

contribution of pensions to per capita household incomes. The share of child benefits and other forms of social assistance, in fact, decreased during the 1980s for all households but marginally increased for households with two or more children.

Indirect transfers in the form of public expenditure on services and transfers in kind (see Table 5.4) are not accounted for in Table 5.5. Nevertheless, the share of wages and salaries decreased by almost 8 per cent for the overall population to 56.5 per cent in 1989 and by 7 per cent

for families with three or more children to 58.6 per cent. This underscores the important and growing role of redistribution in comparison with other countries of central and eastern Europe (see Table 7.1 and 7.2 in Chapter 7). Comparing the structure of 'collective consumption' in certain CMEA countries in 1987 indicates that public expenditures on social provisions in Bulgaria had a similar distribution to other countries of central and eastern Europe (see Table 5.6).

TABLE 5.6 *Structure of public expenditures on social security and social services in CMEA countries in 1987 (%)*

	Bulgaria	CSFR	GDR	Hungary	Poland	USSR
Social security and assistance transfers	50.9	45.3	33.1	59.1	49.4	42.6
Health care	18.2	16.9	18.9	14.3	21.5	15.0
Education & culture	23.1	20.4	20.9	19.6	19.8	23.6
Others	7.8	17.4	27.1	7.0	9.3	18.8
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source: BCSO (1991, pp. 48-9).

Social security cash transfers represented half of public expenditure set aside for social purposes. This reinforces the earlier observation that (a) wages and salaries accounted for less than half of the income/consumption of Bulgarian households, and (b) families in Bulgaria, on average, are probably more dependent on transfers and expenditure of secondary income distribution than in any other country in the region despite the most prevalent egalitarian primary income distribution system. Young families could face irreplaceable income loss if the benefits are removed since the major part of their consumer spending goes towards meeting basic needs. The relative share of food expenditure amounts, on average, to more than 40 per cent of the income of young families, which is the clear sign of a low standard of living. According to surveys, there is a marked insufficiency in the consumption of nutrients vital for the growth of children (especially milk and dairy products, meat, fruit and vegetables).

2. The System of Social Security

Social security and social policy in general have served the following purposes:

a) to redistribute income in an even more egalitarian manner than by the primary income distribution and consumption smoothing;

b) to insure against loss of income due to sickness and accidents;

c) to prevent poverty among vulnerable groups;

d) to encourage population growth.

In order to achieve these goals, the Bulgarian social security system was based on the following principles:

a) universal eligibility for relatively meagre benefits for those with an employment record;

b) all provisions treated as assistance with full discretion of the Party-State and with no differentiation between social insurance and assistance functions and no 'user control';

c) all contributions paid by the employer;

d) differentiation in certain provisions according to the number of children to promote population growth.

Private insurance either for health or pensions does not exist in any meaningful way in Bulgaria and social insurance has been part of the state budget in much the same way as in most other countries of central and eastern Europe (see Chapters 6, 7 and 8). It has not been put on a proper insurance basis, and the only difference between social insurance and assistance was the contribution paid in by the employers. Individual involvement was even more limited than in the Hungarian case (see Chapter 7) inasmuch as the contribution was taken from the wage fund of the employers only, in the form of an earmarked tax, and the salary of the employees was not charged. In the last years, the contribution rate was 30 per cent. During the 1980s, more resources were received in the form of earmarked taxes than benefits paid out, but this surplus had been declining continuously from 2 per cent of GDP in 1981 to 0.5 per cent in 1989. The surplus was transferred to the consolidated state budget, thus leaving no possibility for the social security system to accumulate for hard times at a future date. In real terms, social security contributions increased by about 20 per cent between 1980 and 1988. It declined by 1 per cent in 1989 and by 8 per cent in 1990.

The social security benefits could be grouped into five categories:

a) pensions for the elderly and the disabled;

b) other benefits set out in the Labour Code for employed workers (sick pay, worker compensations, etc.);

c) maternity benefits and family allowances;

d) regular or occasional social assistance;

e) unemployment benefits.

Of these benefits, 96 per cent were funded and administered by the central social security system. All social assistance expenditure (d) was financed by the almost negligible remaining 4 per cent, and was administered by the local councils. Old age and disability pensions (a) accounted for 70 per cent of the total during the 1980s, while maternity benefits and family allowances (c) accounted for 20 per cent, leaving the rest for sick

pay and other benefits (b) prescribed by the Labour Code. Unemployment benefits have existed only since December 1989 and have been financed from a separate fund (0.4% of total social security expenditures in 1990).

Pensions

The standard retirement age is 60 for men and 55 for women — much lower than the average of OECD countries (64 and 62 respectively). In the 1980s, around 25 per cent of the workforce had occupations which entilted them to early retirement (at the age of 50 for men and 45 for women) due to especially dangerous working conditions (for detailed description see Petkov, 1989). Strikes and political pressure resulted in reclassification of a number of professions into these groups. As a result, between December 1990 and March 1991, around 600,000 people (or 15% of the labour force) retired. Until 1991, employment after retirement was permitted. As of January 1991, it was restricted to the private sector.

Pensions are set on the basis of years of service and previous salary. In the 1980s, 25 years of service was needed for men and 20 years for women to qualify for full pension. Pensions varied as a function of service years with a theoretical maximum of 85 per cent replacement rate. Average pensions, however, were very low (around 125 leva per month in 1990, or 80% of the minimum wage) and have not been adjusted for inflation during the 1980s.

The ratio of pensioners to employed was 1 to 2 even prior to the great retirement wave in early 1991 when it increased to almost 2 to 3. The low retirement age allows men to live, on average, 18 years beyond retirement, and women 30 years. In 1990, 60 per cent of old-age pensions were paid to pensioners 60 years old or younger, unprecedented anywhere in the OECD countries.

Accident, illness and death-related benefits

Eligibility for these benefits is dependent on work history and usually prescribed by the Labour Code. Both employed and registered self-employed are covered and become eligible three months after registration. Sick leave is paid for a maximum of six months a year subject to medical verification.

Maternity and child benefits and child-care institutions

There are comprehensive maternity and child benefits in Bulgaria which have been progressive according to the number of children until three children (see Table 5.7).

TABLE 5.7 *Maternity and child benefits per child 1970-1991 (current leva and days)*

Benefit	Unit	1970	1980	1985	1990	1991 [1]
Monthly child benefit until the age of 16 (or 18 for students)						
1st child	Leva	5	15	15/30 [3]	15/30 [3]	115/130/155 [3]
2nd child	Leva	15	25	30	30	130/155
3rd child	Leva	35	45	55	55	155
4th child or >	Leva	5	15	15	15	115
Special provision:		double amount for disabled children double amount and extended until 18 years for single parents increased amount for parents on mandatory military service				
Child birth grant [2]						
1st child	Leva	20	100	100	100	100
2nd child	Leva	200	250	250	250	250
3rd child	Leva	500	500	500	500	500
4th child or >	Leva	20	100	100	100	100
Pregnancy and delivery leave						
1st child	Days	120	120	120	120	120
2nd child	Days	150	150	150	150	150
3rd child	Days	180	180	180	180	180
4th child or >	Days	120	120	120	120	120
Compensation		Full basic wage without bonuses				
Child-care allowance - paid						
1st child	Months	—	6	24	24	24
2nd child	Months	—	7	24	24	24
3rd child	Months	—	8	24	24	24
4th child or >	Months	—	6	24	24	24
Compensation		Minimum wage of the year				
Child-care allowance - unpaid						
All categories	Months	—	—	12 after paid period		
Additional paid annual leave						
2nd child	Days	—	—	2	2	2
3rd child or >	Days	—	—	4	4	4
Compensation		Standard annual leave				
Child-nursing						
All categories	Days	60	60	60	60	60
Compensation		Standard sick pay				

Source: Ministry of Health and Ministry of Labour and Social Welfare (1991).
Notes: [1] As of February 1991. [2] Childbirth grant is discontinued from 15 April 1991. [3] The higher amount is paid for each child after the birth of the second or third child.

Family and child benefits became increasingly comprehensive. In 1985, two years paid child-care allowance was granted and there was an option for a third year of unpaid leave. The job of the parent taking such leave was guaranteed by law.

Child-care institutions occupy an important role in child welfare in Bulgaria. In public crèches (from 9 months to 3 years old) only a small fraction of children (under 10% of the age group) are enrolled, especially after the extension of paid maternity leave to two years. Charges for services, which include food, have been nominal though subject to a means-test (free service for families with less than 40 leva per month per capita). In 1990, for example, the maximum charge in the highest income group was between 2 to 4 per cent of per capita income. The overall cost of the system, in relative terms, was halved between 1981 and 1990, from 0.6 per cent of the consolidated state budget to 0.3 per cent. However, this saving reflected not only decreasing enrolment but a certain deterioration in conditions due especially to decreased investments and delayed maintenance. The problems became acute in the so-called 'mother-and-child houses' where socially endangered children and mothers leave despite the fact that allocations to these institutions doubled during this period.

More than 80 per cent of children 3-7 years old are enrolled in kindergartens, which is not an unfavourable level in comparison with other countries in central and eastern Europe (see Table 1.6 in Chapter 1). Charges were nominal in 1990 with free service for low income families and with a charge of 4 to 8 per cent of earnings for the highest income brackets. Charges for boarding institutions are 20 per cent higher. The overall cost of the child-care system increased in absolute terms but remained steady in relative terms at about 1.7 per cent of the state budget in the 1980s.

Education expenditures made up between 4.5 to 4.7 per cent of GDP during the 1980s. School meals at subsidized rates have only been provided to only less than 40 per cent of pupils because of the shortage of canteens and funds. After-class supervision has not been solved institutionally, thus swelling the number of 'latch-key children' in Bulgaria (see Part I, Section 5 in Chapter 1).

Social assistance for the needy

Social assistance programmes have been administered by the local councils and involved very limited resources (4% of total social security benefits in the 1980s). These benefits are either for special groups such as the handicapped, the elderly without pensions or other forms of income, orphans and families of soldiers, or for the 'socially weak' and include

means-tested lump-sum payments for persons in special distress, subsidies for transport, telephone, drugs, etc. The means-tested benefits include monthly cash allowances and grants for the purchase of drugs on prescription. In 1990, a family was considered 'socially weak' (i.e., eligible for means-tested benefits) if per capita income was under 100 leva per month, or 60 per cent of the minimum wage. The monthly benefits were 100 leva for the first person in a family and an additional 70 leva for each additional person.

Unemployment Benefits

Unemployment is a recent phenomenon in Bulgaria. The first unemployment benefit schemes only started in December 1989. The Professional Training and Retraining Fund (PTRF) set up by the government is responsible for providing two types of unemployment benefit, labour market information and training for the unemployed. All workers dismissed are eligible for benefits. Unemployment benefits are paid on a sliding replacement rate basis. In the first month, the employer is obliged to pay 100 per cent of the base salary, then the PTRF pays the benefit for an additional five months, decreasing it by 10 per cent every month. After six months the unemployed are eligible for unemployment assistance for an additional three months at the level of the minimum wage. This system is now being criticized because it may discourage the labour supply. Families with very low salaries would be better off if one parent were to stop working: the family would then qualify for regular social assistance and the person 'dismissed' for unemployment benefits which, together, could add up to more than the original family income.

The PTRF is financed from two sources: an earmarked tax from the employer which was initially 0.5 per cent and was raised to 3.5 per cent in March 1991, as well as transfers from the state budget.

3. An assessment of the existing social security system

The system was successful in providing a minimum level of social security at a low level of social welfare. Poverty was not targeted *per se* on the basis of means-tested benefits, but a basic income transfer was provided to everyone in the potentially vulnerable groups (those injured in accidents, the handicapped, parents with children, etc.). While this pattern is clearly unsuitable for a more stratified society with serious resource constraints, it was, by and large, adequate in a country where primary income distribution was egalitarian as in Bulgaria.

Social policy, or institutions responsible for social security, cannot be seriously criticized for failing to correct the absurdity of primary income

distribution since social security transfers, by their nature, work towards a levelling rather than a differentiation of income. If income differentiation is increased, it may distort resource allocation further since social security transfers are unsuitable to provide incentives to work.

Criticism cannot be dismissed in the field of the overall welfare impact of social security transfers nor the cost of the system.

It is clear from Sections I and II that social security transfers (in cash and kind) and public expenditure played an unusually large role in providing basic welfare for an unusually substantial part of the population — at least by Western standards. This 'basic welfare' was judged inadequate by the people during the political transition to democracy in Bulgaria. This level is so low that it leaves little room for the economic managers of the country to manoeuvre, as withdrawing benefits would immediately bring large sections of the population not only below the poverty line, but also to the brink of misery.

Despite these paltry results, the system was increasingly expensive. Social security transfers grew from less than 10 per cent of GDP in 1980 to more than 13 per cent in 1990. Their share has been around 20 per cent of the state budget (see Table 5.4). Bulgaria spent more than 8 per cent of its GDP on pensions in 1990, which is 25 per cent higher than Australia, Canada or Japan and more than 50 per cent higher than Portugal or Brazil (though there is a substantial difference in age structure compared with the latter countries). The share of government expenditure on education, culture, health and sport was, on average, around 10 per cent of GDP 1980s which is not high by international comparison (but which conceals substantial disinvestment in human capital and infrastructure and delayed maintenance during the 1980s). Again, there is little reserve left in these sectors after a period of disinvestment in these sectors which unavoidably increases the proportion of GDP when GDP declines. According to very preliminary figures, the share of this expenditure in GDP remained the same in 1990 when production declined by more than 10 per cent compared with 1989 (see Table 5.4).

It should also be pointed out that social policy failed to achieve its pro-natalist goals as well. In the 1980s, the average annual rate of net population growth in Bulgaria was 0.1 per cent, a very low figure indeed as compared with 0.3 in the European Community, 0.7 in developed market economies, 1.1 for the CMEA countries, or 1.8 for the whole world (BCSO, 1991, p. 29). The drop in birthrates has been accompanied by the ageing of the population and the continuous decrease (2% in the 1980s) in numbers of the working-age population (BCSO, 1990, p. 27). The increasing share of GDP expenditure on pensions and the decrease in the working-age population foreshadows a growing financial strain on the social security system.

Having acknowledged that the pro-natalist goals were not achieved, it is also important to state that though social assistance transfers to families did not act as effective incentives to increase family size, they did represent, on average, between 11 and 18 per cent of cash income for families with two children, or three or more, respectively. In the case of poorer families, the ratio is presumably higher and therefore the loss of income, in case of an undifferentiated removal of child benefits would be irreplaceable for them and would bring large numbers of children under the poverty line (for comparison and possible implications, see Table 7.4 in Chapter 7).

II. Transition to the market economy and the adjustment of social policy to radical change

1. Economic reforms in Bulgaria

Bulgaria was regarded as a no-reform country in central and eastern Europe until the political changes began in November 1989 after the replacement of the seemingly unending leadership of Todor Zhivkov. Although the communist leadership was quick to follow the organisational changes periodically initiated in the Soviet Union, the country, unlike Czechoslovakia, Hungary or Poland, did not have its own experience with domestically initiated political and economic reforms pointing towards democracy and the market economy. This has serious implications for the present reform process, both in terms of political support and social and economic know-how.

In addition to the general wave of political change in central and eastern Europe, Bulgaria has been forced along the road to reform by mounting and increasingly unmanageable economic problems. The slow-down and eventual decline in economic growth has been accompanied by rapidly rising convertible currency debts from $3.7 billion in 1985 to $10.4 billion in 1990. Meanwhile, the debt-service ratio soared from the lowest in central and eastern Europe (14%) to the highest (77%) (see *The Economist*, 2-8 March 1991). Capital output ratios increased and shortages intensified throughout the country.

The present reform process in Bulgaria has two distinct phases: slow, gradual change in 1990, and acceleration in 1991.

In the face of the challenge of economic chaos, the old leadership initiated a cautious reform programme in order to reduce macroeconomic imbalances and establish a market economy in January 1989 (by passing Decree No. 56). This decree has served as the legal basis and guideline for reform in 1989 and 1990. The implementation of Decree No. 56 started very slowly and was speeded up somewhat by the new political leadership.

In early 1990, mandatory planning indicators and state purchase orders that guided enterprise operation were abolished; the rights of private ownership (including foreign) were restored and the restrictions on the establishment of enterprises and the limits on the number of employees in them were eliminated; the approval of company managers was transferred back to company boards from workers' councils which, in fact, formerly used to elect the directors; the exchange rates were devalued and the prices of some commodities (10-12% of retail sales) liberalized:

Decree No. 56, and its implementation in 1989-90, proved to be too little, too late. It was inadequate both to stabilize the economy and to provide a comprehensive framework for the transition to the market. As an early sign of its failure, the Bulgarian Foreign Trade Bank (BFTB), with the bulk of the country's debt (85%), had to announce, at the end of March 1990, a moratorium on debt-servicing which was later extended until the end of 1990 and was not reversed even in early 1991 (other banks continue to service 15% of total Bulgarian debt). As a consequence, Bulgaria's foreign trade relations quickly deteriorated, imports fell dramatically which caused unprecedented shortages in consumer and producer supplies and disruptions in production. In order to contain further deterioration in May 1990, a three-tier system of exchange rates (a basic rate for essential goods, a market rate for companies set by monthly auctions and a cash rate for Bulgarians travelling abroad) was introduced to replace the old system of multi-tier exchange rates. In addition, the currency was significantly devalued. According to certain estimates, the devaluation in May alone represented a 'valuation loss' for the BFTB equal to more than 50 per cent of GDP. This will exert huge additional inflationary pressures when debt-servicing will be resumed. Contrary to intention, the system of auctions could not be maintained for long because of the extreme shortage of hard currency. However, a 'Polish solution' for Bulgarian debt problems would be difficult because, unlike Poland, 85 per cent of foreign loans are from private sources. An agreement on cancelling part of the debt with the Paris Club of lenders would be useful but would leave the private loan problem unresolved.

In the second half of 1990, inflation started to accelerate and prices increased by around 85 per cent between May 1990 and January 1991. The Gulf crisis cut Bulgaria off from essential Iraqi oil supplies ($2 bn worth of crude oil remained undelivered in repayment for Bulgarian supplies to Iraq). A complete shift in CMEA trading relations resulted in rapid moves towards hard currency settlements as of January 1991. This involved a trade loss for Bulgaria of between $1.4 and $2.3 billion, or 7-11 per cent of 1989 GDP. Soaring inflation, declining production, disruptive shortages, disarrangement of trading relations, increasing unemployment and a desperate population forced a compromise in the

political process. Thus, the new coalition government embarked on the acceleration of reform at the end of 1990. Gradualist considerations were suppressed by the dramatic situation. Piecemeal reforms were suspended and a radical stabilisation and reform package was worked out and implemented in February 1991. This reform package, though far from being a consolidated blueprint for transition, addresses all major areas of economic change all at once.

In contrast to a three-phase price liberalisation plan which was started and shelved in 1990, the coalition government decided to cut most subsidies and liberalize all prices overnight in January 1991. The prices of only 21 essential commodities remained under state control, but they have been increased dramatically (heating 1,000%, coal 750%, electricity 500%, gas 300%, etc.). Most consumer and producer subsidies were cut. As a consequence, prices more than doubled in February alone (205%) and the index of food prices jumped by 286 per cent between January and February. The food price index stood at 443 per cent in February compared with May 1990, whereas the overall price index was 380 per cent. The relative price of food (food price index compared with non-food consumer price index) increased by 31 per cent between May 1990 and February 1991, and by almost 70 per cent in February 1991 compared with January 1991. Households with a higher share of expenditure on food (especially families with young children) suffered more than others.

Dramatic changes have been implemented and are underway in the labour markets. Price rises in 1990 were followed by certain adjustments in nominal wages (between December 1989 and July 1990, average wages increased on current prices by 10%). The sharp decrease in real wages in the second half of 1990 prompted labour disputes and industrial action with certain results. According to an agreement between the political parties, trades unions and the government, partial compensation was provided to wage earners in February 1991 for the price rises. The compensation was in the form of a wage supplement which is subject to government decision, whereas base wages were left unchanged until May 1991 when wage-setting would be liberalized and steeply progressive wage taxes applied (e.g., any increase in the overall wage fund of an employer in excess of 3% would be subject to an 800% wage tax). The wage formula applied in February aims to secure 70 per cent of the social minimum for everybody. A linear monthly supplement of 270 leva is paid to every employer, thus bringing the actual minimum wage up to 435 leva ($31 at the official exchange rate and around $15-20 per month on the black market) from 165, although this latter figure remains the legally binding minimum. The average monthly wage increased to 600-650 leva ($40-45 at the official rate or $30-35 at the unofficial rate). According to Ministry of Finance calculations, the overall cost of the wage supplement is

7 billion leva and only a fraction of it will come back in the form of payroll taxes. Around 70 per cent of the planned budget deficit is expected to be the result of wage and benefit supplements. Pensions have been supplemented by 182 leva and most other benefits by 100 leva.

Partly due to strikes and political pressure and partly in preparation for renewed labour market structures, the government accepted requests from various labour groups for early retirement. As a consequence, 600,000 people, 15 per cent of the labour force, retired during the three months between December 1990 and February 1991, thus cutting the labour force from 4.9 million to 4.3 million. A further contraction of the active labour force to 3.6 million at the end of 1991 is expected due to further retirements and increasing unemployment. The number of unemployed stood at 100,000 in February 1991, or 2.5 per cent of the labour force. But this number is expected to rise to between 350,000 and 400,000, which will be around 10 per cent of the labour force at that time.

In order to offset the decrease in tax revenue due to the decline of production and the shrinking labour force, the government increased and diversified the rate of the formerly linear social security contributions (similar to a payroll tax) from 30 to 35, 45 or 50 per cent according to expected years of service in a particular occupation (the shorter the service the higher the contribution rate). The contribution to the unemployment fund has increased seven-fold from 0.5 to 3.5 per cent and changes in the amount and eligibility of unemployment benefit are also contemplated. Critics of the existing scheme argue that it constitutes a disincentive to the labour supply and is too expensive. It is that the sliding replacement scale (see Part I, Section 3) will be modified by a lower flat rate for the whole period of unemployment.

In order to increase competition, a decision was taken in March 1991 to dismantle the 79 largest monopolies into smaller units by the end of April 1991. These large companies had failed to respond to liberalisation and subsidy reduction other than by increasing prices. An anti-trust law is currently under preparation. Small business activities are encouraged. The number of small companies increased from 33,500 in July 1990 to 80,000 by January 1991. Firms are no longer subjected to central export targets, and this is expected to increase supplies and competition on the domestic market (moreover, CMEA obligations are being phased out in 1991). Despite the severe shortage of foreign currency and continued inability to service the country's debt, a decision was taken to aim at a Polish-type internal currency convertibility. In principle, all registered economic enterprises are allowed to change leva into foreign currency and conduct foreign transactions. In practice, however, every claim is subject to clearance by the central bank. As part of the efforts to create the

conditions for domestic convertibility and import competition to curb inflation, shops selling for hard currency should shift to domestic currency as of 1 April 1991. The plans for internal convertibility are based on the assumption that the IMF will assist the radical reform by granting an initial $1.3 billion loan in the first half of 1991. (However, by March 1991, the agreement had not yet been concluded.)

Privatisation requires a longer period of time. After early efforts in the tourism sector in April 1990, the government suspended the sale of all state assets in August 1990 until final decisions were taken on legislation. A law on the reprivatisation of land was carefully worked out and passed in the parliament on 23 February 1991 with much less political controversy than anywhere else in central and eastern Europe. This law gives land back to the original owners with guarantees and obligations to secure its cultivation. Privatisation of industry and services may start in the second half of 1991 if work on the law is finished and the bill adopted.

Financial and capital market reforms are under way. The main aims are to strengthen the role of the National Bank as a central bank responsible for monetary policy and to modernize the operations of the commercial banks. From the end of 1989, the imposed specialisation on commercial banks has been lifted which is essential to increase competition. Inflation produced largely negative real interest rates in 1990. Lending and deposit rates were increased substantially in February 1991, but it remains to be seen if positive real interest rates can be achieved. Development of capital markets will follow the stabilisation efforts and possibly it will be linked to the implementation of privatisation. The government expects that privatisation will play an important role in eliminating 'monetary overhang' in the economy by providing an alternative to inflationary measures.

2. Shock Therapy with a Difference?

The second phase of economic reform which started in February 1991 is very similar to the Polish shock therapy in its radicalism (see Chapter 8). Indeed, certain elements (such as speed and degree of institutional change) may prove to be even more radical. Despite this, the Bulgarian experiment receives far less attention from the international media and little support from the international community. The reason for this mixed reception is the controversy over the social dimension of the changes, which are inherent in the Bulgarian reform. The World Bank and the IMF have criticized the preliminary versions of the reform package on three grounds:

a) that it contains large compensation for price rises which are expected to turn inflatory;

b) that it does not reduce the costly social security programs;

c) that it does not raise low retirement age, thus imposing an unmanageable strain on the budget and on pension payments.

Against this backdrop, it is necessary to draw attention to the following considerations:

Unlike Poland, the implementation of the radical reform package in Bulgaria was not preceded by a protracted period of high inflation. Both the structure and the level of prices required a one-time adjustment in one great leap due to the lack of earlier reforms (and inflation). This task could not be solved by tight monetary policy because the conditions (i.e., missing institutional background for the required monetary and fiscal policy and the accumulated monetary overhang) did not allow for it.

On the other hand, both the absolute level and the distribution of income and employment structures (see Sections I, II and III) were unable to absorb the full extent of damage caused by the one-time application of austerity measures and the leap in price levels without certain compensation. For example, without adjustment, the minimum wage would have bought less than 2 kg of medium quality sausage, or 5 kg fatty meat per month. In February 1991, the adjusted minimum wage could buy almost 5 kg of the same sausage (milk and sugar were still not available easily despite the eight-fold increase in price). As in Poland (see Chapter 8), compensations represent only partial indexation (70%). If such meagre compensations can be seen as overheating from a theoretical economic point of view, it should be recognized, from a practical social point of view, that any *overheating* is taking place in a deep-freezer. The government's intention was that compensations would not overcushion the transition but avoid overkill.

The political process brought about a rapid articulation of group interests which did not have adequate time for discussion and compromise. Political and industrial disputes imposed binding agreements on the coalition in the second half of 1990. The governing coalition has a strong mandate for general economic changes (e.g., retirement categories) in legislation and for stabilisation, but with almost no mandate for change in the relative position of the various social groups. People, in principle, accepted the idea that markets should be created and that their well-being would be affected, but they could not accept large differences in the starting conditions (neither would it be at all easy for macro economic management to decide what market wage scales should be).

Some of the allegedly avoided reductions in costs and services, in fact, took place despite the compensations even if only in relative terms (e.g., the nominally increased child benefits bought only half of the amount of milk in February as it did in January 1991). The planned deficit

of the budget in 1991 is seven-fold compared with the 1990 plan, but it is not much higher in real terms.

The retirement-unemployment trade-off may prove erroneous if it is not seen as a temporary, or rather emergency, measure (adopted rather unwillingly by the government). It is expected that the short-term dislocation of the labour force due to restructuring will be even greater in Bulgaria than elsewhere in central and eastern Europe. The industrial structure of the country is more obsolete than in most other countries of the area and its dependence on guaranteed exports to the shrinking markets of the Soviet Union is excessive. Also, the present and prospective influx of foreign capital falls far short of investment in Czechoslovakia, Hungary and Poland. This limits still further the short-term possibilities of creating new employment. For the moment, at least, Bulgaria is not confronted with problems of quantitative labour supply, nor its relative cost (it is one of the cheapest in Europe). But it does face unemployment problems which could easily get out of hand with all of its economic and political consequences. The issue of the cost of the decision could be seen in the context of the fact that despite the seven-fold increase in the contribution rate of unemployment insurance, the financial burden of the unemployment scheme would remain, at least partially, in the budget as will the cost of pensions. In the long-term, however, there is little doubt that retirement conditions also need to be updated and pensions cannot be treated as some kind of 'last-resort employment'.

III. The social dimension of the transition and the new model of social policy

1. The social impacts of the reform

The first phase of the reform in 1990 already had to contend with serious social implications, although clearly most of these could be associated more with the overall economic crisis than the reform measures themselves. As a consequence of subsidy reductions and lack of imports due to the moratorium on debt servicing from March 1990, unprecedented severe shortages could be observed. Out of 295 goods monitored on the domestic market, the supply of 225 items (75%) was behind 1989 levels. The supply of sugar to the consumer market was reduced by almost two-thirds and that of baby food by 71 per cent. Meat, milk and eggs disappeared from shops and, often, even rationed goods proved to be unattainable. Lack of imported fodder and grain caused animals to starve. The number of cattle decreased by 12 per cent in 1990 compared to 1989 and negative changes in the same order of magnitude threaten pork and poultry as well.

Disruption due to the lack of imported spare-parts and extreme restrictions on imports in general resulted in a 70 per cent gap between moderately estimated needs for and supplies in baby milk. Imported medicines, sometimes irreplaceable, became extremely scarce. This was especially detrimental to children. Infant mortality, after decades of improvement, started to increase again in 1989 and, according to preliminary indications, this negative trend was not reversed in 1990 either.

Real family income declined in 1990 despite a certain increase in nominal wages due to accelerating inflation which caused a drop in overall consumption. There were reports of deterioration in the dietary status of certain social groups, usually with more children than average, as food prices rose and shortages intensified. Both kindergarten and crèche enrolment rates declined substantially in 1990 and early 1991 because many families found it difficult to pay increased fees.

Unemployment appeared as a social problem for the first time in 1990. The number of unemployed rose from virtually nil to 2 per cent of the labour force by the end of the year.

Public construction activities dwindled in 1990 due to further decreasing capital expenditures, which further aggravated the housing situation. Already 16 per cent of families (with some 40% of all children) live in sub-rented lodgings. Half of the children in Bulgaria do not have their own room.

Changes in February 1991 have had even more dramatic implications, even though soaring 'market clearing prices' (see previous section on the February price-shock) reduced shortages and there were substantial compensations. Basic foodstuffs, such as bread, milk and dairy products, increased in price by factors of between six and ten. Milk and sugar were still in short supply two months after price liberalisation (queuing continued for these items in shops). Despite compensations which aimed at offsetting 70 per cent of price rises, real income was almost 50 per cent down compared with the previous year. According to government calculations, the number of people living in or on the verge of poverty may reach or even surpass 50 per cent within months. The real implications of the price shock will be seen when households run out of stockpiled food and have to turn to the market.

The scarcity of foreign exchange and imports became even more acute. Vitamins and certain antibiotics disappeared from chemists because former CMEA trading relations were shifted to a hard currency basis as of January 1990. Because of the lack of vital drugs and imported spare-parts for equipment, some health establishments may have to suspend their activities (e.g., gynaecological interventions, cardiac surgery, etc.).

From May 1991, the liberalisation of labour markets may cause substantial income differentiation and may swell the number of vulner-

able groups. Unemployment has rapidly increased and could reach 10 per cent of the labour force by the end of 1991. However, the real value of unemployment compensation may not be guaranteed due to increasing strains on the unemployment fund and the budget.

2. The quest for a new model of social policy

There is no agreement, yet, about what kind of social security system would be desirable in the new Bulgaria. It seems, however, that there is an understanding that overcoming the existing shortcomings cannot be achieved by a careless destruction of the existing system. Its reform should instead aim at adjusting to the concrete stabilisation efforts, economic constraints and transition properly and immediately, and should create capacities to adjust to the more long-term needs when these can be clearly identified and agreed upon. It is likely that the new system will emerge more as a result of step-by-step adjustments and not as a result of the implementation of a radically different blueprint. The most counter-productive measures should be removed and new forms and mechanisms for social insurance and assistance corresponding to the new needs should be introduced.

The general principles guiding the reform of social insurance are: increased cost-sharing in the form of increased and more individual contributions and higher users fees, freedom of choice and competitiveness in financing and social service provisions; independence, self-government and self-support of the system. A bill is being prepared in this respect, and it is expected that the social insurance fund or its functionally separate elements will become independent later on in 1991. In particular, a three-tier system of financing is proposed for health care in which state budget funds, separate self-financed and self-governed health insurance funds and private funds and charities would be involved. Those elements of the system which allow choice could be financed by increased private involvement, whereas the more indivisible elements would be based on broader public support. A more personal form of contribution to compulsory health insurance than the payroll tax on employers is seriously being considered. In service provisions, an independent from the source of financing, competition should be encouraged in order to increase the efficiency of the system.

The agenda for child health care contains emergency elements as well, such as meeting the urgent necessity for overcoming the drastic shortage of formula food for children, drugs and medical equipment and more institutional ones (e.g., for the integration of disabled children into the society). The transition requires the assessment of corresponding risk factors and flexible institutional and policy responses, and also the activa-

tion of new domestic and foreign channels to assist child health care.

The increase in the number of pensioners and the *de facto* lowering of effective retirement age, as discussed earlier, do have negative implications for the budget and for the future pension fund. It should be clearly understood, however, that this result was not the original aim of the government (see Section II).

The reform of the social security system will require different inputs to deal with means-testing, universal (including family) benefits, and subsidies.

The need for targeted, *means-tested social assistance* is expanding with the deterioration in living conditions. This seems to be a cheaper means of alleviating the problems of the most vulnerable groups and its importance can and should increase as differentiation of income in primary distribution accelerates sometime after May 1991, and as universal schemes may prove inadequate both in terms of financing needs and their appropriateness. Important institutional changes are needed, however, in order to target social assistance more efficiently as the methods of means-testing are under-developed and there is no network of social workers (in the modern sense) in Bulgaria.

What can the poorest members of society expect in 1991? Families and persons with an average per capita income of less than 65 per cent of the minimum wage, including the 270 leva compensation, can apply to local social assistance bodies for monthly benefits which will bring their income up to the indicated minimum amount (435 leva). Similar assistance is foreseen for children in specially difficult circumstances and for children of unemployed parents. A new feature is that this social assistance is to be provided predominantly in kind, namely, in the form of coupons for free meals or to meet expenses for utilities. In order to increase the scope of social action in this field, the government approved, immediately after the price reform of 7 February 1991, the setting up of a new fund for social assistance.

The current universal schemes are unavoidably being put into question because of their cost and unfocused character. At this stage of the reform (i.e., February 1991), they were widely applied and reinforced in the form of wage and benefit supplements and because the overwhelming majority of people found themselves in serious need as a result of all the recent political and economic changes. It seems clear that means-tested programmes are cheaper than universal ones if the number of potential recipients is limited — which was certainly not the case in February 1991 when, without compensation, 85 per cent of Bulgarian workers would have fallen below the poverty line (see Table 5.2).

There is no full compensation for child-related benefits either. Socially-insured (i.e., employed) mothers receive the usual maternity and child-

care allowances (see Table 5.7) and an extra monthly compensation of 242 leva until the child is two years old. Subsequently, 90 leva compensation is paid until the child is three years of age. A compensation of 100 leva per child is payable along with the usual amount of child benefit until the age of 16 years. The one-time birth grant will be eliminated on 15 April 1991. Unemployed mothers are in a less favourable situation. They have been receiving so far only 10 leva assistance from local councils. They will now receive, in addition, 90 leva compensation (which, of course, is not sufficient to cope with rising prices).

Although pro-natalist benefits did not achieve their purpose, they became indispensable elements in most family budgets. Meanwhile, the cost of these benefits and allowances increased from 2.6 per cent of GDP in 1980 to almost 3 per cent in 1990 (BCSO, 1990, p. 131). The issue of income replacement could not be overlooked since the majority of families would fall below the poverty line even if the original rationale of these benefits proved to be faulty. It may be that, for the time being, they may remain the most convenient way of keeping families above the poverty line. However, as primary income differentiation progresses, this approach will need to be changed.

Producer and consumer subsidies were largely phased out during the February 1991 reforms and subsidies are no longer seen as a desirable means of social welfare. However, the issue of certain child-related subsidies remain pending. The question is whether such support as formula for children, drugs or clother should continue. In 1990, the cost of these subsidies reached 0.26 per cent of the state budget and still only about 30 per cent of domestic needs were met in the case of crucial child formula items. In the absence of hard currency to import substitutes, a hands-off policy would be irresponsible. This is especially true in cases where import or foreign assistance are temporarily unavoidable.

The increasing awareness of civil society with regard to social problems, and activities of the church and NGOs are likely to lend support to charity activities, though perhaps to a lesser extent than elsewhere in central and eastern Europe due to different traditions and a lower level of private accumulation. However, these initiatives (e.g., soup-kitchens, distribution of second-hand clothes to the needy, etc.) are welcome and social policy should strive to accommodate them.

The monitoring of living standards and of vulnerable groups became crucial to the success of reform and political consensus. The government, parties, unions and other groups of interest should be able to follow closely developments in this area. The Central Statistical Office therefore established a new unit to issue monthly consumer prices and cost-of-living indexes for the public and for the National Commission for Coordination

of Interests which regularly reviews compensations and other areas where social assistance may be needed.

3. The problems and effects of poverty alleviation of the new social policy

The biggest problem facing economic and social spheres in Bulgaria is the extremely reduced room for manoeuvre in policy-making due to binding resource constraints and low income levels. According to the estimates used in the process of setting the criteria for wage and benefit supplements, 38.6 per cent of the population lived at or below the poverty line prior to the reform in February 1991. Since the compensations have been only partial at 70 per cent of the initial price rises and subject to renegotiations in June 1991, again when wage liberalisation is expected to take effect (supplements are not regarded as part of base wages) the relative share of people living at or below the poverty line is likely to swell to at least 50 or 55 per cent of the population which will naturally include many active persons in the labour force — quite apart from the soaring number of unemployed. In 1990, the number of people in need of social assistance and social care was about 1.8 million, or nearly 20 per cent of the population. The economic crisis and ensuing unemployment will further raise the proportion to 25 per cent, placing still greater strains on budgetary expenditure to provide protection for the socially vulnerable.

This generalising of poverty threatens the reform of social policy inasmuch as it may block the way towards leaner, more targeted programmes, increase the need for income transfers from the shrinking GDP and thus may hinder the success of the overall economic and political transition. There are no guarantees that the agreement on under-indexation can be kept during 1991, nor that a self-destructing political confrontation will not erupt. Moreover, hyperinflation could effectively wipe out the hope for an orderly reform of the social security system which should be rebuilt out of the ashes after a painful *tabula rasa*. But, it is well known that ash does not make good bricks.

CHAPTER 6

CHILDREN AT THE TURNING POINT: ECONOMIC REFORM AND SOCIAL POLICY IN CZECHOSLOVAKIA

Alena Kroupová with Ondřej Huslar

Iures and shortcomings of socialist social policy

The social situation in Czechoslovakia today is characterized by two different but closely related problems, namely, the failure of the former socialist system to provide adequate social security and social assistance to all inhabitants; and the necessity of facing up to the social conflicts and tensions which resulted from the economic reforms initiated in mid-1990 and early 1991.

The first section of this chapter deals with the former problem, while the latter is discussed in Sections III to VI.

1. MAIN FEATURES OF SOCIALIST SOCIAL POLICY

As in other socialist countries of central and eastern Europe prior to 1990, social policy in Czechoslovakia was characterized by:

a) Full employment of practically the whole working population;

b) Centrally regulated wages characterized by relatively modest differentials between the highest and lowest;

c) State-financed social security including almost universal provision of a large number of benefits in cash and kind;

d) Subsidies on food, rents and other basic goods enjoyed by all the population;

e) Universal and free (or strongly subsidized) provision of services in the health care, education, child care and other social sectors;

f) Limited scope of and generally inflexible approach to social assistance.

Under the socialist regime, the system of social security, health and education — which took shape gradually over the last three decades and which is still largely in existence in early 1991 — was fairly developed and absorbed a large and growing share of federal, state and local government budgets (Table 6.1). During the 1980s, social expenditure absorbed

between 47 and 53 per cent of total consolidated government expenditure, a ratio similar to or higher than that of the developed market economies of western Europe. However, there were serious imbalances between its main sectors.

TABLE 6.1 *Consolidated public expenditure by major categories*

	1980	1985	1986	1987	1988	1989	1990[3]	1991[4]
	A. *Billions of current crowns*							
General admin.	6.5	8.2	8.5	8.5	8.9	8.9	8.0	10.8
Defence	22.9	27.4	28.3	28.5	29.2	43.8	43.8	39.7
Economic activities	130.5	117.3	116.6	124.3	133.6	119.5	112.4	87.1
Social expenditure	144.3	186.5	193.6	201.4	209.3	222.2	214.7	268.4
— health	20.2	25.6	27.9	29.4	31.1	33.2	37.0	41.6
— education	22.3	26.8	27.9	29.1	30.5	31.7	32.0	38.9
— other[1]	31.3	46.8	48.1	51.8	53.8	57.8	42.6	80.8
— social security	70.5	87.2	89.7	91.1	93.8	99.5	103.1	107.8
of which:								
pensions	43.8	55.1	56.7	58.1	60.1	64.5	—	—
sick pay	7.0	8.6	9.1	8.8	9.2	10.0	—	—
child & family benefits	19.1	22.8	23.1	23.4	23.6	24.1	—	—
miscellaneous[5]	0.6	0.7	0.8	0.8	0.9	0.9	—	—
Other[2]	—	18.7	19.1	19.5	20.1	20.5	58.5	58.4
Total consolidated public expenditure	304.2	358.0	365.9	382.2	401.2	414.9	437.3	464.4
	B. *Percentage shares*							
General admin.	2.1	2.3	2.3	2.2	2.2	2.1	1.8	2.3
Defence	7.5	7.7	7.7	7.5	7.3	10.6	10.0	8.8
Economic activities	42.9	32.8	31.9	32.5	33.3	28.8	25.7	18.8
Social expenditure	47.4	52.1	52.9	52.7	52.2	53.6	49.1	57.8
— health	6.6	7.2	7.6	7.7	7.8	8.0	8.5	9.0
— education	7.3	7.5	7.6	7.6	7.6	7.6	7.3	8.4
— other[1]	10.3	13.1	13.1	13.6	13.4	13.9	9.7	17.2
— social security	23.2	24.4	24.5	23.8	23.4	24.0	23.6	23.2
of which:								
pensions	14.4	15.4	15.5	15.2	15.0	15.6	—	—
sick pay	2.3	2.4	2.5	2.3	2.3	2.4	—	—
child & family benefits	6.3	6.4	6.3	6.1	5.9	5.8	—	—
miscellaneous[5]	0.2	0.2	0.2	0.2	0.2	0.2	—	—
Other[2]	—	5.2	5.2	5.1	5.0	4.9	13.4	12.6
Total consolidated public expenditure	100	100	100	100	100	100	100	100

Source: State Budget, FMF (1990); FMPSV (1990a).
Notes: [1] Sports, housing subsidies, local services, environmental protection, etc. [2] Until 1980, different classification. Breakdown not available. [3] Preliminary. [4] Proposed. [5] Social assistance and funeral subsidy.

In the early 1980s, social security expenditure represented 18.9 per cent of GDP, the seventh highest ratio out of 26 highly industrialised countries. While ranking behind countries such as Sweden, Denmark and France (which allocated between 22 and 28% of their GDP to social security), Czechoslovakia ranked well ahead of all other socialist countries, as well as market economies such as Italy, the United Kingdom, and the United States (Gordon, 1988, Table 2.1).

The main features of social policy and the main benefits and provisions were as follows:

a) Pension benefits were universal (and included agricultural workers). There was a strong accent, however, on equalisation which, while introducing a strong element of solidarity, penalised those with relatively higher wages and social security contributions. In addition, replacement ratios were rather low, so that many pensioners received benefits well under 50 per cent of their last salary. Sick-pay benefits were also universal and relatively generous.

b) *Family policy* was — and still is — fairly comprehensive. It included a vast array of benefits and services which were designed to tackle rapidly falling birth rates, increasingly unstable family relationships and the need to incorporate women into the labour force. The most important of these cash benefits are summarised in Table 6.2. There were additional, if less common, benefits for the wives and children of soldiers, scholarships for student-mothers, and benefits for pregnant women unable to work at their workplace among others.

c) For those mothers and families who opted not to take advantage of the child-care allowance (see Table 6.2), there was the possibility of placing children in *state-financed crèches* (which by 1989 included 95,000 children, i.e., around 18% of the 6- to 36-month age group) or, for those with older children, in *kindergartens*. Kindergartens had a longer tradition and high enrollment rates which grew from 82 per cent in 1980 to between 94 and 97 per cent between 1985 and 1989. Tuition and school meals were basically free of charge. Indeed, between 1985 and 1989, an average of 85 per cent of children in kindergartens and of pupils attending compulsory schools took advantage of highly subsidised school meals.

The comprehensiveness of child and family policy in Czechoslovakia in the 1980s is underlined also by the existence of other measures such as *income tax relief* for families with children, as well as rent and transport subsidies.

The value of benefits in cash and kind and of indirect provisions to families with children remained considerably stable (in constant terms) during the 1980s, with the exception of the increase between 1980 and 1985 in child allowances and school meals, due to the 1982 and 1985 food price rises (Table 6.3, panel A). By 1989, they exceeded 40 billion crowns,

TABLE 6.2 *Cash benefits for families with children*

Benefit	Duration	Amount (per month unless otherwise stated)
1. Maternity benefit	28 weeks (37 weeks for single mothers)	90% of previous salary
2. Childbirth grant (as of 1-1-1991)	—	3,000 crowns
3. Child-care allowance (for father or mother)	Up to 3 years of age for each child	900 crowns
4. Child nursing benefit (for father or mother)	Up to 7 days every illness episode	Equivalent share of full salary
5. Benefit for the handicapped child		500-700 crowns
6. Child allowance and educational benefit	Up to 26 years old	
for 1 child		200 crowns
for 2 children		650 "
for 3 children		1,210 "
for 4 children		1,720 "
for every further child		350 "
7. Subsidised loans for young couples	—	50,000 " (at marriage)

Source: FMPSV (1991).

equivalent to 9.7 and 5.6 per cent respectively of consolidated government expenditure and of the Gross Material Product (GMP). The value of the average transfers per child/month was quite substantial and represented about 15 per cent of the average monthly salary. The value of the transfers increased to about 25 per cent if transfers to mothers were included (Table 6.3, panel B). These figures compare favourably with those of OECD countries where, in 1987, family benefits (including transfers and tax relief, but excluding benefits in kind, which account in Czechoslovakia for about 20% of total transfers to families) represented 13 per cent of the disposable income of an average one-earner family. Only in Austria (18.4%), Belgium (19.9%), Germany (14.5%), Luxembourg (23.4%) and Norway (16.5%), as well as Hungary (see Chapter 7, Table 7.2), were family transfers (as a proportion of salaries) commensurate to those of Czechoslovakia (Kamerman and Khan, 1991). However, the high relative value of child/family transfers should be seen in relation to the low level of Czechoslovak wages, of which, according to the

TABLE 6.3 *Social assistance to families with children*

	1980	1985	1986	1987	1988	1989
A. *Billions of current crowns*						
Direct cash benefits	19.62	23.41	23.44	23.49	23.76	23.76
including:						
— child allowances	14.08	16.42	16.40	16.26	16.17	16.50
— educational benefits	—	0.94	0.92	0.92	0.93	0.49
— maternity benefits	1.90	1.91	1.90	1.99	2.10	2.11
— maternity allowances	1.36	1.64	1.68	1.70	1.75	1.75
— birth grants	0.49	0.44	0.44	0.43	0.43	0.41
— nursing benefits	0.60	0.88	0.95	0.99	1.21	1.32
— state subsidised loans	0.53	0.46	0.45	0.45	0.41	0.41
— scholarships	0.38	0.35	0.29	0.29	0.28	0.28
— other	0.27	0.37	0.40	0.46	0.48	0.49
Benefits in kind	6.59	7.95	8.12	8.38	8.61	8.84
including:						
— creches & infant homes	0.77	0.92	0.87	0.89	0.87	0.86
— kindergartens	2.69	2.99	3.05	3.15	3.24	3.36
— school meals	1.34	2.28	2.39	2.45	2.55	2.60
— youth homes	0.94	0.74	0.76	0.81	0.89	0.93
— other	0.85	1.02	1.05	1.08	1.06	1.09
Indirect transfers	6.95	7.43	7.51	7.52	7.56	7.61
including:						
— income tax relief	5.99	6.45	6.54	6.60	6.65	6.71
— transport subsidies	0.62	0.65	0.65	0.64	0.64	0.64
— rent subsidies	0.34	0.33	0.32	0.28	0.27	0.26
Total assistance to families	33.16	38.79	39.07	39.38	39.93	40.21
B. *Per beneficiary and in relation to wages and total expenditure*						
Average benefit per child (crowns/month) [1]	373	440	438	439	449	458
Average total support per child & mother (crowns/month) [1]	648	729	729	737	754	775
Average wage in state & cooperative sector (crowns/month)	2637	2883	2927	2987	3054	3123
Total family assistance (as percentage of total government expenditure)	10.00	10.80	10.70	10.30	9.90	9.70

Source: FMPSV (1990a).
Note: [1] Calculated from the figures above.

socialist wage theory, they constituted an essential component. From this perspective, high transfers did not represent a laudable achievement but, rather, an irreplaceable necessity.

Families with several children and only one income-earner received close to half of their disposable incomes in the form of transfers in cash or kind and of indirect transfers. In the case of families facing multiple deprivations (handicaps, single-parenthood, divorce, etc.), the value of the transfer was even higher and accounted for between one-half and two-thirds of household income. This is an important conclusion which ought to be considered when discussing the future social policy.

d) *Social assistance* was little developed. There were means-tested benefits paid by local authorities for those who did not qualify (because of lack of employment or other reasons) for the near-universal child allowance and maternity employment-related benefits described above. There were also supplementary means-tested benefits for the old and the handicapped and for foster children. All together, social assistance absorbed only 0.2 per cent of total government expenditure (Table 6.1).

Finally, *health care* (including maternal and child care) was provided virtually free of charge by the National Health Service. Drugs were provided free of charge (except for a small handling charge), although there were important shortages, particularly for imported drugs. Ten years of *compulsory education* was also provided free by the state to all children. Books and teaching aids were also free, while, as mentioned, school meals were provided at highly subsidised prices. Other activities (youth clubs, summer camps, etc.) also received financial support from the state. High school, vocational training and university education were also free of charge, although they covered only a fraction of the young in that particular age bracket.

This complex array of social transfers and public expenditure were completely financed, *de facto*, by the public budget, even if, formally, there were separate accounts for government expenditure, social security payments and social assistance. Public expenditure was rather centralised. The federal and state budget accounted for about two-thirds of total budgetary expenditure (Table 6.4). Because of the nature of the budgetary process in centrally-planned countries (according to which the resources for education, health service, social security, etc. were allocated simultaneously by the Federal Government, by the Czech and Slovak Republics and by the local authorities), it is not immediately possible to break down consolidated government social expenditure into expenditure by federal, state and local government. Family benefits, in contrast, were covered entirely by the Federal Government. In the near future, however, the state budgets of the Czech and Slovak Republics are expected to play a larger role in this field.

TABLE 6.4 *Budget expenditure according to type of government (billions of current crowns)*

	1987	1988	1989
Central Government expenditure	245.2	258.4	263.1
(of which)			
— Federal Government	66.9	72.4	70.2
— Czech Republic Government	110.4	115.8	118.4
— Slovak Republic Government	67.9	70.1	74.5
— Local Government expenditure	137.0	142.8	151.8
Total Consolidated Government expenditure	382.2	401.2	414.9

Source: FMPSV (1990a).

2. SHORTCOMINGS OF SOCIALIST SOCIAL POLICY

As argued in Chapters 3 and 4, the failure of the socialist experiment was most pronounced in the political and economic spheres. Distributive and social policies, however, while less affected by systemic or efficiency problems, have also been characterised by major difficulties. Broadly speaking, the objective of social justice for all never was nor could ever be achieved. To start with, such an objective did not reflect the real needs of the population, but rather the paternalistic decisions of the Party State. In addition, social policy was limited by the poor performance of the economy which failed to introduce much needed policy reforms and which continued to be heavily dependent on the performance of the less-developed neighbouring socialist countries. And, finally, the pursuit of such objectives led to the formation of a highly centralized political and administrative system which by itself represented the denial of the ideals of personal choice, social security and welfare and equal chances for all.

Despite important progress, particularly in the 1950s and 1960s, in the fields of public health and universal access to education and social protection, such an approach caused a number of acute problems and distortions which are as follows:

Stagnant labour productivity, stifling of incentives and suppression of private initiative

The policy of artificially imposed full employment generated a large number of inefficient jobs which depressed overall labour productivity and technical progress. At present, labour productivity does not reach half that of western European countries; while, before World War II, Czechoslovakia had one of the highest levels of labour productivity in the world. The stagnation of productivity has certainly represented a major obstacle to the growth of wages and to the scope of redistributive policies.

In addition, the central regulation of wages led to their general levelling out and to the stifling of incentives to work and private initiative. Wage discrimination against intellectual and professional activities, which were frequently less remunerated than manual labour, also led to limited progress in technical innovation and scientific research. And, finally, because of the low level of average wages, the survival of the average family depended on both parents going out to work — a fact, as will be seen below, that has caused severe problems.

For instance, while average monthly wages in the 1980s oscillated around 2,500-3,000 crowns (Table 6.3), the basic needs of a typical four-member family was estimated at approximately 4,000 crowns (Struk, 1990). Young couples with families with wages well below average were especially obliged to rely on two incomes.

Erosion of family cohesion, distorted values and social deviance

As a result of the policy of full employment, 48 per cent of the total population was employed throughout the 1980s. As female employment was proclaimed to be a woman's main expression of equality with man, women have traditionally represented 47 per cent of the working population (UVVM, 1989). At 98 per cent, the present employment rate of women in the 20- to 50-year-old age bracket is one of the highest in Europe — as is, of necessity, the proportion of children in state-financed pre-school facilities.

The emphasis on full employment as the main goal for every individual and the strong role persistently advocated by the Party State in child socialisation — despite the reforms of 1964 and of the 1970s — seriously affected the role of the family whose social, cultural and educational functions were substantially reduced. This situation contributed to the erosion and growing instability of the nuclear family, and to the weakening of solidarity between generations, the under-estimation of citizens in post-productive age and, frequently, to a belittling attitude towards their needs. The weakening of the family role was compounded by a tendency to place children from problem families under the 'protective supervision' of state institutions, rather than trying to solve the problems of the family through proper social support. Of the children in institutions — who represent 1 per cent of the respective age group — only 2 per cent were complete orphans, while only 10 or 3 per cent, respectively, were adopted or placed in foster families (Struk, 1990).

The weakening of the family and its educational role in family planning, compounded by a shortage of a suitable means of contraception and by the negative side-effects of measures aiming at providing housing on a priority basis to young couples with children, contributed greatly to

exceptionally low levels of contraceptive use and to exceptionally high levels of abortions and/or of very early parenthood. Indeed, Czechoslovakia has one of the highest ratios of induced abortions (Table 6.7), one of the lowest average age for mothers giving birth, one of the highest proportions (80%) of children born within eight months of the wedding and one of the highest rates of divorce (FSU, 1990a). All this, in turn, fueled family instability, the institutionalisation of children, and an increase in juvenile delinquency (Report on the Status of the Czechoslovak Family, 1991). Indeed, children born to very young parents, from problem families, or raised in institutions are more likely to experience, later in life, high rates of juvenile delinquency.

Erosion of the real value of expenditure and social benefits

Free health care and education in the 1950s and 1960s did improve the standard of education and contribute to the lowering of infant mortality. However, expenditure on social security, health care and education which appears to have grown slowly in current prices during the 1970s and 1980s (Table 6.1) has, more likely, stagnated, or even declined, if account is taken of the (modest) growth of population (around 0.2 or 0.3% a year), of the slow aging of the population, of the greater health expenditure needs caused by the rapidly deteriorating environment and of 'shortageflation' (i.e., inflation resulting from both official price changes as well as 'repressed' inflation resulting from shortages of goods for which substantially higher prices were paid on parallel markets). Conclusive evidence on the decline or stagnation of social expenditure cannot, however, be given. While official inflation (that reflecting price changes on the official market) increased by only 12 per cent between 1980 and 1989, there is not yet a reliable assessment of *overall* shortageflation.

During the 1980s, the nominal value of most social security benefits, including employment-related benefits, were kept constant. Their real value did not therefore keep pace with the gradual increase in the cost of living and salaries. In 1970, for instance, maternity allowance represented 31 per cent of the average woman's salary, while it had declined by 1989 to 22 per cent (Sbírka Zákonu, 1990). Child allowances, in particular, did not keep pace with the growth in the cost of living for young families with more than one child (Table 6.5). Because of this distortion, families with two or more children faced a greater and growing risk of falling into poverty. As a result, despite a relatively vast array of social benefits, in 1988 about 9 per cent of children were living in families with incomes below the social minimum (Kovarik, 1988).

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TABLE 6.5 *Net per capita income by number of children in the family (income of one-child family = 100)*

Number of dependent children in the family	1980	1988
Two	82.4	81.4
Three	71.8	71.5
Four and more	59.1	58.3

Source: FSU (1990c).

The gradual deterioration of the economic situation of families is indirectly confirmed by the increase in the total social assistance expenditure for means-tested benefits for child nutrition and for pregnant women. This is a good indication of the growing number of families facing a severe risk of poverty (Table 6.6).

TABLE 6.6 *Social assistance benefits paid to families (millions of crowns per year)*

	Child nutrition benefit	Benefit to and pregnant women
1985	72	44
1986	84	59
1987	91	110
1988	93	121
1989	90	152

Source: FMPSV (1990a).

Inadequate old-age pensions — which neither kept pace with the cost of living nor with salaries — were also responsible for the gradual pauperization of many pensioners. So, despite continued full employment and the virtually total coverage of old-age benefits, the proportion of pensioners living below the poverty line increased from 8.3 per cent in 1980, to 8.9 per cent in 1985 and to 9.5 percent in 1988 (FSU, 1990b).

The relative neglect of health care

Though slowly growing, public health expenditure (practically the only one in existence) has been relatively low in relation to market economy countries. In the 1980s it remained, on average, well below 4 per cent of GDP (FMF, 1990) as compared with an average of 7 to 7.5 per cent in western market economies (Kamerman and Khan, 1991). The health sector, in addition, had to fulfill the functions of a non-existent social

assistance, while having to deal with the health hazards caused by the conspicuous lack of health-nutrition education and the absolute neglect of basic environmental protection (Czechoslovakia accounts for one-fifth of the total industrial emissions for 15 noxious substances in Europe as a whole). While life expectancy at birth over the last 20 years has stagnated (or even declined) for men and improved only marginally for women, there has been a clear increase in child morbidity (respiratory infections, allergies and tumor diseases) (Table 6.7). While medical treatment has partially compensated for this increased morbidity, the ensuing slower decline in the infant mortality rate (IMR) has caused a deterioration in the position of Czechoslovakia in the worldwide ranking of countries by level of IMR (see Chapter 1). In addition, the high morbidity rate of children overburdens the health care services which are forced to devote themselves more to medical care than to health promotion.

TABLE 6.7 *Selected demographic indicators (1960-1989)*

	Incidence of tumors in children below 14 years of age [a]	Artificial abortions per 100 births	Life expectancy at birth (years)	
			men	women
1960	—	40.2	67.6	73.1
1970	100 [b]	43.3	68.2	72.9
1980	209	40.0	66.8	73.9
1987	226 [c]	56.0	67.6	75.0
1988	229	75.9	67.8	75.4
1989	—	76.1	67.6	75.2

Sources: FSU (1990a); FSU (1990b); FSU (1982); FSU (1980); Struk (1990).
Notes: [a] 1975 = 100; [b] 1975; [c] 1985.

Grossly inadequate, under-financed and inflexible social assistance

In spite of continuous public pronouncements, the social assistance needs of the citizens went unrecognized and represented merely the 'residual' element of the state budget. In 1989, it accounted for about one billion crowns, or 0.2 per cent of total consolidated government expenditure (Table 6.1 — see also Chapter 2). The number of social workers for general and case work was very limited, as there was no higher education in social work, and the number of students in related secondary schools was artificially limited. Social assistance work was mainly of an administrative nature and, in many cases, it limited itself to the provision of financial help. Prevention and the search for problem cases was not carried out. Assistance was provided according to uniform schemes which did not foresee catering to particular needs or individual cases. Indeed,

because of their formalistic and impersonal nature, the situation of persons in need grew worse. In addition, the unified and centrally directed system of awarding services and benefits had very high overhead costs and was therefore highly inefficient from an economic point of view.

A complex range of social services is still missing. The situation of handicapped people is particularly difficult because of inadequate provisions and the lack of understanding on the part of the public. Many of them could not participate in public life because of architectural barriers, lack of wheelchairs, lack of amenities for visually or auditory handicapped people and a lack of special workshops. Even now, there is no legal obligation to employ the handicapped, or to pay higher mandatory contributions whenever this duty cannot be fulfilled. Despite the cash transfer to handicapped children (Table 6.2), these children were largely dependent on institutional care as both their parents — even those able and willing to care for them — were obliged to join the labour force because of the low level of wages.

Growing sense of dependence and passivity

Finally, the centralization and paternalism of socialist social policies created a strong sense of dependence among the population and limited the capacity and willingness of the individual to provide for his or her life and to feel responsible for his or her family. Such dependence and passivity cannot be abolished by an administrative measure.

The task of educating people to take responsibility for their lives and for those of their families is, ironically, made difficult by the encouragement of the previously suppressed free expression of one's views. The steps taken by the new authorities, possibly not always the best ones, irritate the still surviving attitude of the past in the minds of the young and the middle-aged, that 'someone above' is responsible for their welfare. This creates social tension and could possibly jeopardise the economic and social reforms which depend on the active participation of the population for their success.

II. Economic reforms: basic principles and initial implementation

The economic reforms introduced in Czechoslovakia include three main components: price liberalization, privatisation and liberalization of foreign trade based on limited domestic convertibility of the currency.

According to *The Scenario of Economic Reform* (FS, 1990), all three main elements described above were to be implemented simultaneously from 1 January 1991. 'Small-scale Privatisation' by the auctioning of state shops was to have started in the autumn of 1990. But because of delays in

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the Federal Assembly caused by discussions about the sharing of responsibilities between the Federal, the Czech and the Slovak governments, its implementation was postponed until January 1991. Privatisation of large enterprises (and former church land) is a more complex — and therefore slower — process both from the technical and political points of view. One option being considered entails their financial and structural transformation into joint stock companies whose shares would either be sold or exchanged for 'investment coupons' thus entitling all citizens to purchase shares at much reduced prices (because of low savings by individuals in relation to the market value of these enterprises). Another option would be to restitute all property nationalised (legally and illegally) between 1948 and 1989 to their former owners or their heirs.

By the end of February 1991, the parliament had approved a Land Restitution Bill, returning property *illegally* nationalised between 1948 and 1989 (about 10% of former private property) for an estimated value of 300 billion crowns (approximately $10 bn). A decision on the various options is expected to be taken when the 'Big Privatisation law is enacted.

Price liberalization — mostly concerning food prices — started on schedule, although it does not yet apply to rents and energy prices nor has it yet created a competitive economic environment. Indeed, price liberalisation has led to a sharp increase in food prices whose index (based on a basket of 240 items) rose in Czechoslovakia by 34.4 per cent during the first two months of 1991. The increase was caused mainly by the rise in trade margins of monopolistic trade organizations that do not have to compete yet with private shops. A sharp rise in the price of food resulted in a drop in demand which seems to have dampened, in turn, the growth of prices. There are also cartel practices among different producers and different trade organizations because of the delayed enactment of the Antitrust Law which was only approved by the Federal Assembly on 30 January 1991. The delay was caused by disputes among the Federation and the two Republics on whether there should be one, two or three antitrust laws and offices.

Liberalization of imports has not yet influenced competition on the domestic market, as the (gradual) reduction of import tariffs has yet to start. In the meantime, the currency has been devalued on several occasions (including 20% in January 1991), while limitations on the purchase of hard currency by Czechoslovaks are going to be lifted during 1991.

These reforms have been supported by anti-inflationary stabilisation measures, introduced in 1990 and accentuated in 1991, the most important of which are restrictive fiscal and monetary policies. Over the medium term, these fiscal measures will be accompanied by a thorough tax reform, the main elements of which will be income tax and a value added tax which will replace the present turnover tax. As part of these

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restrictive fiscal policies, food subsidies were withdrawn in mid-1990. An *ad-hoc* universal and undifferentiated benefit of 140 crowns per month was granted to compensate partially for the price increase triggered by the withdrawal of subsidies. In addition, major cuts in production and consumer subsidies for energy and rents will take effect during 1991. An industrial reform programme — including the gradual closure of factories which are environmentally hazardous or producing armaments — is also expected to come into effect, although less clear commitments have been made in this area.

Stabilisation and privatisation measures are aimed, in particular, at reducing the total consolidated public expenditure in real terms and as a share of the Gross Material Product; achieving a budget surplus; and changing the structure of budgetary outlays by reducing defence expenditure and production subsidies to enterprises more than to all other categories.

The extent of such measures is best assessed on the basis of the data in Table 6.8 which provides information on public expenditure in constant 1988 prices (obtained by deflating the data in Table 6.1 by means of the Consumer Price Index with base 1988) and a few other macroeconomic indicators. It clearly appears that, while continuing to grow until 1989, total public expenditure declined by 4 per cent in 1990, while it is expected to contract by another 17 per cent in 1991. Although GMP declined in 1990 by 3 per cent and is projected to decline further by 2 per cent in 1991, there was a drop in the GMP/public expenditure ratio in line with the objective of reducing the role of the public sector in the economy. Finally, in 1991, the government will attempt to keep aggregate demand — and inflation — under control by aiming for a budget surplus of about 1 per cent of GMP which is close to 2 per cent of public expenditure.

All major categories of expenditure have been affected by the fiscal austerity of 1990 and 1991. Indeed, while expenditure levels and structures hardly changed between 1985 and 1988 (Table 6.1), the moderate growth of expenditure in 1989 was accompanied by a sharp increase in defence spending (its real volume was first acknowledged only in 1989) and by an initial 10 per cent decline in expenditure on economic activities (including mostly subsidies to enterprises on account of the difference between domestic and foreign import-export prices, and subsidies to agriculture). Such structural change has been accentuated in the 1990 and 1991 budgets which show a major decline in subsidies to enterprises and in defence spending, accompanied by a smaller but real decline in public expenditure on social services and transfers to the population.

The net effects of the above changes on the overall structure of public expenditure have been profound (Table 6.8, panel B). The relative decline

TABLE 6.8 *Consolidated public expenditure in constant prices and by main categories*

	1988	1989	1990 [1]	1991 [2]
A. *Billions of crowns at constant 1988 prices*				
General administration	8.9	8.8	7.2	7.5
Defence	29.2	43.3	39.4	27.5
Economic services	133.6	118.2	101.1	60.2
Social services and transfers	209.3	219.8	193.1	185.6
Other	20.1	20.3	52.6	40.4
Total consolidated public expenditure	401.2	410.4	393.2	321.2
B. *Percentage shares*				
General administration	2.2	2.1	1.8	2.3
Defence	7.3	10.6	10.0	8.6
Economic services	33.3	28.8	25.7	18.7
Social services and transfers	52.2	53.6	49.1	57.8
Other [3]	5.0	4.9	13.4	12.6
Total consolidated public expenditure	100.0	100.0	100.0	100.0
Memo items:				
Budget surplus (deficit)	2.8	0.5	4.8	5.5
Total public expend/GMP ratio	—	61.5	58.4	48.6
GMP growth rate	—	1.0	−3.0	−2.0
Official inflation rate (on CPI)	0.1	1.1	10.0	30.0

Source: Elaboration of data in Table 6.1.
Notes: [1] Preliminary; [2] proposed; [3] FMF and FMPSV (1991).

in the share of economic services and defence spending has been compensated by the rise in the share of social expenditure and social security transfers.

It is important to note that the above-mentioned reforms have received strong political support and that provisions have been made to reduce their social costs (see Section VI). A major step forward was the general agreement established at the end of January 1991 between the Federal Government, the Republics, employers' associations and trades unions on minimum wages and wage indexation.

The progress of reform in the economic and social field is being closely monitored. The Federal Government approved a system of monitoring the performance of the Czechoslovak economy. The important indicators for measuring the social impact of the reforms are: the different types of price indexes; the cost of living indexes; and the incomes and savings of population. These should also suffice to monitor the situation of the most vulnerable groups, namely, families with small children and old-age pensioners.

III. Problems emerging and expected

The political, economic and social transformation of Czechoslovakia is so recent that any discussion of the social impact of such measures at the time of writing (in early 1991) is hardly possible. Moreover, the relatively favourable economic conditions (e.g., a strong industrial base and low hard currency debt) as compared with the other countries of central and eastern Europe and the cautious approach adopted so far, should spare the country any major economic upset or the social tensions experienced for instance by Poland and Hungary.

In spite of this, the transition to the market economy presents serious social risks, even in Czechoslovakia. These include unemployment, inflation (with the ensuing erosion of real salaries, pensions and benefits) and the contraction, or higher costs of key public services. While even a steep decline in income and service provision could be borne without major problems by a relatively affluent society such as Czechoslovakia, difficulties could arise, however, if the burden of cuts in employment, income and social services were distributed unequally. A few specific social groups — already in a difficult situation because of the inadequacy of socialist social policies, or because of their employment in sectors particularly affected by the reforms — stand to suffer disproportionately. Among them are pensioners, families with more than two children and single-parent families, youth in search of first-time employment, unskilled workers, and minority groups. Furthermore, during the transition, or at least during its early phase, it will not be easy to find a solution to the problems inherited from the previous regime which were mentioned in Section I. This is bound to frustrate some of the expectations raised by the recent political changes.

In the initial phase of the transition, the real incomes of most social groups are expected to decline. In 1990, per capita GMP dropped by an estimated 3 per cent and is expected to decline further by at least another 2 per cent in 1991. Unemployment has grown from 20,000 people (half of them receiving some unemployment benefit) at the end of July 1990 to 80,000 people in February 1991. Unemployment will rise as price and trade liberalization and further reduction of production subsidies take effect. While the efficiency of most enterprises will improve, not all of them will succeed in adjusting to the new conditions. They will, therefore, have to close down. Unemployment is expected to affect about 200,000 people by mid-1991 and about half a million by the end of the year and in 1992 (Struk, 1990). In the case of rapid privatisation of large enterprises, it could, however, reach 800,000 people, or more than 10 per cent of the labour force (*Financial Times*, 6 February 1991). Elderly and unskilled workers, particularly if working in low-productivity sectors (e.g., defence

and heavy industry), will be severely affected. Both these groups and their families include a considerable number of children. Families with an unemployed parent are a quite new phenomenon in Czechoslovakia. In addition, because the centralised vocational training system is still in operation, high school and university graduates will suffer most from unemployment.

The anti-inflation policy which was agreed upon by a large majority of political parties and movements foresees only a *partial* indexation of wages, pensions and benefits (even if inflation reaches high rates) as a way of avoiding an uncontrolled price-wage spiral. While this is a necessary feature of the overall stabilisation policy, its social cost would become unbearable if inflation were to reach, say, three-digit figures. While, as previously mentioned, inflation rose to 34.7 per cent during January and February 1991, the government is expecting the consumer price index to increase by up to 70 per cent by December 1991.

In 1990, public expenditure on cash transfers to households declined by about 6 or 7 per cent. Expenditure on education dropped by about 10 per cent, while sport, housing and ecology received some 35 per cent less. Only in health did expenditure rise (by about 4%). As a result, a number of user charges (for nurseries, school books, etc.) were increased in 1990. However, it is not clear as yet if the demand for these services has shrunk. The situation had already deteriorated in 1990 in the field of drug supplies, as the disintegration of the state pharmaceutical monopoly and the shortage of credit and foreign exchange resources combined to make the traditional chronic shortage of drugs even more acute. Real government expenditure on health, education and cash transfers to the household sector are expected to decline further in 1991 by about 20, 10 and close to 20 per cent respectively (see Table 6.9).

A number of special measures — illustrated in detail in Sections IV to VI — have been enacted to deal with these risks. Nevertheless, despite such provisions, there is a distinct danger that the social situation may deteriorate during the period of the transition, particularly in case of:

— a substantial increase in inflation, which — because of the type and frequency of indexation chosen — could greatly depress the living standards of the poor;

— possible large-scale bankruptcies accompanied by large-scale job losses;

— further deterioration of the economic situation as a consequence of external reasons (further rises in the price of oil, world recession and a further breakdown of CMEA trade);

— different rates of development of the Czech and Slovak economies which may lead to growing migration and tensions;

— insufficient resources to deal with the devastation of the environ-

ment and the near-exhaustion of natural resources — another legacy of the past economic development model and one which requires immediate and expensive measures if further and irreparable environmental damage is to be avoided;

— lower than expected foreign loans and direct foreign investment.

IV. The new social policy model

The reform of social policy in Czechoslovakia is expected to correct the most severe distortions and injustices inherited from the previous regime while introducing into the new social security system some new elements specific to a market economy. In addition, social policy has the task of minimising the social tensions arising — temporarily — from the transition to the market economy. The achievement of these interrelated, though separate, objectives will not be easy and will be influenced by pressure-group demands for unattainable results and by the overall political process.

Social policy is expected to proceed along two parallel tracks. First, measures have been and are being taken to set up the new social security system which is expected to be fully operational only by 1993. Second, as part of this broad reform, a number of measures — often referred to as social *safety nets* — have been rapidly put into place to tackle the immediate social problems arising from the transition to the market economy. The new overall social security system is described below and in Section V, while the safety nets are discussed in Section VI.

1. The new long-term social security model: general principles

The new overall social security model illustrated below was prepared by the Czechoslovak government (HN, 1990). It was agreed upon after tripartite negotiations with representatives of the Trades Union Confederation and of the Confederation of Employers, and is based on five principles: universality, liberalization, democratization, efficiency, and decentralization of social assistance.

According to the new system, all members of society will participate in future social policy. It will be necessary to establish different levels of tasks and responsibilities for individuals and the state, as well as the limits of state intervention.

The basic level will be formed by *citizens for themselves*, namely, the active care of the individual for his or her own life and family. At the second level, *the citizen in collaboration with the state*, the state provides the basis of the system, but the onus is on the individual to choose the degree of participation (e.g., additional insurance). The third level, *the*

state for the citizen, is made up of all measures guaranteed by the state to its citizens in order to ensure a minimal standard of living. This level will secure the framework for solidarity with those in need, underwrite family policy and ensure social assistance. Thus, the state undertakes that no family will fall below an established level of absolute poverty.

Social policy in Czechoslovakia will ultimately combine universal services and benefits, as well as those services provided selectively and in individual cases. It represents a combination of the principle of universality and selectivity on behalf of individuals in particularly difficult situations. The state will continue to play a decisive role in establishing the level of a number of *universal* subsidies and services when responding to the needs of the majority of the population (e.g., child allowances) and *selective* subsidies when resolving special situations (e.g., handicapped children, etc.).

Private initiative and voluntary aid are also new elements in social policy. Legal regulations will be enacted to enable private persons and institutions to start activities in the sphere of social welfare. It is expected that with state aid, these institutions will broaden the range of social services offered to families and will provide for the needs of special groups to which the state is incapable of responding.

A prerequisite for the success of social reform is the decentralization of the administration of services and budgets. Local elections in November 1990 ratified the independence of local authorities which now have responsibility for their own budgets. Until then, all social benefits and services were part of the state budget and local authorities were allotted funds from the central government according to given criteria. With the new reform, it will be possible to complement these funds with local taxes and charges on individuals and enterprises which can be used for regional development or for special social benefits and services. The overall level of these benefits will therefore be influenced both by local development programmes and by programmes financed by the central authorities. This is the case, for instance, with the state family policy, as agreed by the Federal, the Czech and the Slovak Governments.

2. Adapting the existing elements of social security

Many former elements of social security will be carried over. Among them are the following:

a) Labour market policies will change drastically. Under a tripartite system, the state will limit itself to overseeing labour agreements between the employers' associations and the trades unions which will set basic conditions such as the length of the working week, minimum wages, or safety and health on the job. The state will also ensure implementation of

mandatory international conventions. With the new policy, wages will depend on productivity. Wage discrimination in sectors such as public education, health and social assistance will gradually be removed. In heavy industry (particularly in mining and metallurgy) — where preferential wages were prevalent and where important retrenchments are planned — the retraining of the labour force and psychological support to cope with the loss of employment and income is necessary.

b) Most of the social services and benefits of the socialist system will be maintained. The basis for the entitlement, however, will shift as many of the provisions become social insurance-based.

In addition, there will be a greater differentiation in social provisions, which — while ensuring basic services and benefits to everybody — is expected to increase the quality of the services received or the value of benefits for those paying a higher premium, or who have hazardous jobs or are willing to bear the cost of additional (private) insurance. Among the main changes expected, those concerning *pension insurance* is the most important. Under the new system, the state will guarantee the first component, namely, a universal minimum pension (calculated in relation to the minimum standard of living or absolute poverty line) even for the long-term unemployed. The second component will be represented by the part coming from compulsory employment- related insurance of all citizens and which will depend on their wage level, the premium paid and the number of years of employment. The third component of the pension will be formed by compulsory insurance of enterprises where continuous exposure to health risks occurs, and by additional voluntary private insurance.

Another important amendment of the existing pension system concerns the gradual increase of minimum pensions and of average replacement ratios which — as seen in Section I — are often rather low. The first two revisions of pensions were carried out in October 1990 and March 1991.

c) Sick-pay benefits will no longer be drawn from the health care insurance fund, but from the payment of sickness benefits by the insured. Basic changes in this respect should concern only the abolition of the income ceiling which determines the calculation of sickness benefits.

d) The health care system will also undergo transformation. The National Health Service (financed by state budget) will be replaced by the compulsory health insurance of every individual — employment and income-related — assuring both basic and specialised health care of appropriate quality. A further improvement in the quality of the health service could become available to those willing and able to pay for additional health services. Means-tested patient contributions might be requested also for those health services which are particularly expensive or of long duration. This new framework — which is being hotly debated

at present — would provide not only improvements in health care, but also a greater interest by doctors in the treatment of patients. Everyone would bear responsibility for his or her own health. The new system, inspired by those in operation in Germany, Austria and in the Netherlands should help to increase the total expenditure on health care, which, as seen above, has traditionally been rather low (FMF, 1990) and for which modest provisions were made in the 1991 state budget (Tables 6.8 and 6.9).

e) The framework of state family policy will also change. Instead of providing mandatory assistance to families (in practice, only to those with dependent children), social policy should rather aim to create the conditions necessary for families to help themselves according to their special needs and possibilities. Greater individual freedom will help to foster a higher sense of responsibility for family living conditions and foresight during times of crisis (see Section V).

f) The provision of ten years compulsory education free of charge will be safeguarded by the state. A new law has granted independence to universities and all lecturers are now free from any state tutelage. The recent law on autonomy in education gives the schools the chance to enjoy a higher degree of decentralisation. The law enables communities to found basic schools. Private and church schools are not subject to the state at all, but whatever education is provided as part of the compulsory ten-year cycle should be supported financially by the state.

3. Introducing new components of social policy

With the transition to the market economy, new benefits and social institutions must be created while some of the old ones have to be adapted to meet new circumstances. Among them are the following:

a) Unemployment benefits were introduced in Czechoslovakia in 1988 under the name of *allowance before employment*. The new proposal presented to the government redefines unemployment. It concerns citizens permanently residing in Czechoslovakia who have applied for employment regularly to the appropriate authority which cannot provide it within seven days. The unemployment office provides the applicants with unemployment benefits while searching for suitable employment or appropriate training courses.

Unemployment benefits (HN, 1991) represent at least 65 per cent of the average monthly wage received during the last employment period for the first six months and 60 per cent for the second six months (HN, 1991). For persons gainfully employed independently, the subsidy is calculated from paid up insurance contributions. For all those not included in either case, the unemployment subsidy is equal to the minimum

pension for those without any other source of income (in March 1991, it was equal to 1,440 crowns per month) (see HN,1990). During the period of unemployment benefits, the recipient may be employed in casual labour. After 12 months, the recipient becomes eligible for social assistance. Over the past three years, the unemployment subsidy has been financed by the state budget. For 1991, a reserve of 2 billion crowns has been foreseen in the national budget (to cover up to 400,000 unemployed throughout the year with an average benefit of 2,000 crowns a month). Later on, the unemployment fund will become gradually independent as contributions from employees and employers create the necessary reserve.

b) The concept of a minimum wage was introduced at the beginning of 1991. The minimum wage legislation, which concerns every category of worker, will be provided irrespective of productivity or the capacity of the employer to pay. It corresponds to the wage tariff of basic manual work. The minimum wage for 1991 is construed as to ensure remuneration above the absolute poverty line and is expected to increase in line with living costs during 1991 and the expected changes in income tax.

c) Wage indexation is currently under discussion and three mechanisms are being considered. First, the adoption of conditions agreed by collective bargaining to cover minor increases in the cost of living. Second, the adjustment of wages whenever inflation exceeds 5 percentage points by an amount which is under discussion (but which would anyhow be less than the observed inflation rate). Finally, through special *ad hoc* wage benefits.

d) A new element is constituted by the indexation of all social benefits. According to preliminary discussions, this would be introduced in the event of a 5 per cent increase in the average wage and in case of a 10 per cent increase in the cost of living. The estimated expenditure for this provision, which concerns families with children, represents some 3 billion crowns per year, or about 1 per cent of the state budget. These allocations were agreed upon as a minimum figure together with the visiting World Bank mission in January 1991, but they have not yet been included in the 1991 state budget. Putting aside adequate resources is, however, crucial and will require a fundamental decision from the government following tripartite negotiations between the representatives of the government, the Confederation of Trades Unions and the Confederation of Employers (General Agreement of the Czechoslovak Government, 1991).

e) In Czechoslovakia, social assistance has traditionally been geared towards helping families with children, the aged or the handicapped who were below minimum living standards (Section I). With the transition to a market economy, some adaptations and extensions will be necessary. First of all, periodic adjustments of the absolute poverty line will be required to

keep in line with changes in the cost of living. This will, in turn, entail the upward adjustment of individual benefits and the introduction of means-tested subsidies for housing costs for families with unemployed parents no longer eligible for unemployment benefits, for handicapped children and adults without adequate insurance or any means to pay. In addition, social assistance will have to provide regional services to stimulate local-level social-development programmes (HN, 1991). Resources for these activities, however, have not yet been included in the state budget for the year 1991.

4. Financing the new social policy

Under the previous regime, all social benefits and services were financed by the state budget, except for a minor private additional insurance. There was no clear separation between the various social insurance funds. The reform of the financing of the new social security system is expected to be completed at the same time as the tax reform, namely, by 1 January 1993. Social security contributions will be deducted directly from personal income tax. All together, income tax, unemployment, sickness, pension and health insurance will account for between 20 to 25 per cent, on average, of the gross income. A separate and independent social insurance fund will be created which will be fed with the social security contributions of employees and the self-employed. The state social insurance fund, on the other hand, will be fed by general taxation and private contributions. The ratio of participation by the employers in these funds is still under consideration.

As a first step, it is estimated that in 1991 and 1992, approximately half the present contributions from income tax to the state budget will be hived off to form the basis of the social insurance fund.

V. Child and family policies

It is most likely that the greatest impact on family welfare will result from the reform of the labour market, as well as income and social insurance policies. Changes in child and family policies and benefits are, however, expected to play an important role, particularly for those families with two or more children or who are affected by other social risks (e.g., single parents, presence of handicapped family members, etc.). These families, prior to the political and economic reforms of 1990 and 1991, already depended on public transfers for more than half of their disposable income and, at the same time, experienced the highest incidence of poverty in the country (see Section I).

The new family policy respects and develops the unique bonds of the

human being to his or her family environment. While ensuring a greater freedom of choice for all family members — and women in particular — in their decision to join the labour force, the state will continue to guarantee, through the Social Solidarity Fund, benefits or grants for maternity, birth and children. Moreover, the benefits for child nursing or for seriously handicapped children will be maintained. All benefits are universal and parents and children can claim them regardless of their income if they are Czechoslovak citizens living in the country.

Some of these benefits will have to be reformulated such as child allowances, at present paid by the sickness insurance scheme, and which depend, to some extent, on the employment record of the parents and on the number of children in the family. Amending these discrepancies will take two years and will be carried out at the same time as the tax reform, so as to compensate for the withdrawal of the current wage tax-relief for children.

Further means-tested benefits for families will be maintained within the framework of social assistance, of which the most important are those for child nutrition subsidies, housing benefits, and fuel allowances.

State-supported services are an important tool in the care of children. These include creches, nurseries, kindergartens, school meals, free textbooks and school materials, low fees in halls of residents, youth homes and reduction in fares (Table 6.3). It is calculated that the costs of kindergartens, school meals and youth establishments will be supported by the state as a form of general solidarity during the transitional period. However, according to local conditions and funding, user charges will be introduced according to the quality and type of services provided. In addition, the free supply of textbooks and school utensils will be limited. Families will be expected to pay approximately 50 per cent of costs. It should be pointed out here that former free use has led to an underestimation of the real value of these materials and to their misuse or destruction. None of this contributed to fostering a sense of responsibility.

As it is necessary to ensure free medical care for mothers and children at the present relatively high level, a part of the new programme will continue to ensure free supplies. However, with the growing differentiation due to the introduction of multi-tiered health insurance systems, certain drugs will be fully or partly paid for by patients. In spite of all this and of the fact means-tested subsidies for health care are granted by local authorities (whose resources vary considerably), it is hoped that universal access to child health care will remain an absolute priority under the new health system.

As has already been mentioned, subsidies on food and other household articles for children have been or are being withdrawn. At present, there is still a certain amount of state support for certain basic foodstuffs

(such as milk). However, this is more of a subsidy towards agricultural production than relief in favour of children. But, even this was reduced during the opening months of 1991.

The complex concept of state family policy will find its complete expression in a new law on family support (FS, 1990b) which will be promulgated by the beginning of 1993. In addition, the ratification of the Convention on the Rights of the Child by the Czechoslovak government will oblige it to prevent undue stress on children and their families during the transition to the market economy (UNICEF, 1989). It is hoped that, in spite of the present uncertainty, the existing (and future) legal obligations will help protect the interests of children over and above the particular interests of individuals, political parties and pressure groups (FS, 1990b).

VI. Social safety nets

While the overall reform of social security is likely to be completed by early 1993, the Czechoslovak authorities have already passed a series of measures which are consistent with the new social security system being developed. These will ensure that no undeserved pauperisation of children or other social groups will occur during the long and difficult period of transition to the market economy. The rapid introduction of social safety nets is a prerequisite for the amendment of the Czechoslovak social legislation in accordance with the Social Charter of the European Community. This is a necessary step for future full membership in the Community.

The concept of safety nets, namely, a set of income maintenance and other measures intended to prevent poverty, revolves around that of minimum family income or *absolute poverty line*. The absolute poverty line is defined by a level of income which represents about two-thirds of the social minimum (HN, 1991) and about one-third of average disposable family income. For a four-member family with two children, for instance, the monthly social minimum amounts to 4,800 crowns, while the absolute poverty line can be estimated at 3,200 crowns. Average disposable family income (including transfers) is estimated at between 7,000 and 8,000 crowns per month.

The social safety net which has been put into place is largely based on the social assistance sub-system and includes:

- a minimum wage (2,000 crowns per month in February 1991);
- unemployment benefits;
- social assistance to families with children and needy persons;
- increase in pensions for those with no other source of income;
- social assistance;
- social assistance for institutional care.

Thanks to the introduction of a minimum wage, unemployment benefits and the amendment of minimum pensions, a minimum family income ought to be ensured for all families with at least one breadwinner or an old-age pensioner.

To protect families against the risks of inflation, the social minimum and child allowance will be adjusted so as to cover the cost of basic food and other minimum requirements. Together with the increase of this limit, allowances will be adjusted every time wages increase by 5 per cent (HN, 1991).

Minimum pensions for those with no other source of income will be adjusted whenever the cost of living increases by 10 per cent (HN, 1991).

Because of the previous low level of rents, privatisation of the housing stock and the abolition of housing subsidies could have devastating effects for low- and middle-income families, particularly for large families and old-age pensioners.

In order to safeguard the housing rights of low-income families, no legal amendments or increase in rents should be allowed to threaten socially accepted basic needs. Special housing guarantees will be provided for handicapped persons and means-tested rent and utility subsidies will be ensured by social assistance. In addition, an *ad hoc* benefit will be provided upon the withdrawal of the energy subsidy. Finally, religious and private organisations are expected to contribute particularly in the case of personal assistance to vulnerable groups.

The effective implementation of the above measures depends on the creation of appropriate public bodies and regulations and adequate financing in the state budget.

It is too early to judge the resilience and efficiency of the network of public bodies and private organisations charged with the provision of social assistance. In the case of prolonged or high unemployment, or persistently high inflation, such a system will be severely strained.

The 1990 and 1991 consolidated budgets have already provided financial coverage for some of the above measures. It is estimated that the cost of compensating for a 10 per cent increase in the cost of living will amount to about 3 billion crowns and will concern some 4.2 million children and some 7,000 adults. The most important of these financial provisions concern unemployment subsidies and the cost of retraining workers and an *ad hoc* compensation for price increases in food and energy for certain population groups. As already mentioned, however, an important part of the expected public expenditure for the indexation of family benefits and social assistance had not found the necessary financial coverage in the state budget by early 1991.

These new allocations for safety nets accounted for 3.1 per cent of the total public expenditure in 1990 and 9.5 per cent in 1991 (excluding

the allocations for social assistance which cannot easily be separated out in the data of Table 6.9). While part of the resources for these activities are obtained from savings on building subsidies and 'other' items (see last line of Table 6.9), about two-thirds of the resources are obtained by squeezing the real value of expenditure on health, culture, education and, in particular, social security transfers.

TABLE 6.9 *Composition and structure of social expenditure*

	Bn current crowns		Bn 1988 crowns		Shares of total gov. exp	
	1990 [2]	1991 [3]	1990 [2]	1991 [3]	1990 [2]	1991 [3]
Social expenditure	214.7	268.4	193.1	185.6	49.1	57.8
of which:						
Social security [1]	99.7	115.3	89.6	79.7	22.8	24.8
Health	37.0	41.6	33.3	28.7	8.5	9.0
Education	32.0	38.9	28.9	26.9	7.3	8.4
Culture	6.4	7.9	5.7	5.5	1.5	1.7
Compensation for food price increases	13.5	27.0	12.2	18.7	3.1	5.8
Compensation for energy increases	—	7.5	—	5.2	—	1.6
Unemployment and retraining	—	9.9	—	6.9	—	2.1
Rehabilitation of victims of communism	—	1.5	—	1.0	—	0.3
Building subsidies	9.6	3.0	8.6	2.1	2.2	0.6
Other [4]	16.3	15.9	14.7	11.0	3.7	3.4

Source: FMF (1991).
Notes: [1] Slightly different definition than in Table 6.1; [2] preliminary; [3] proposed; [4] includes subsidies for science, sport, environmental protection and the state budget reserve.

VII. Safety nets and expected effects on poverty

There will be inevitable social consequences resulting from the unavoidable but necessary economic reforms initiated in mid-1990 and early 1991. Even if it is much too soon to perceive any impact, it is possible to make a few observations on the new social security system and the safety nets.

First, the overall design of the new social policy, if not yet completely delineated, seems to be fairly comprehensive. Despite the strong shift towards insurance-based services and benefits, the multi-tiered system envisaged ought to be able to retain a universal character while aiming at increasing efficiency and personal responsibility. The system, however, could become excessively dualistic if the universal basic benefits decline substantially in real terms because of inflation. While the better-off could further expand the private insurance component of their own social

security, the system as a whole would become excessively fragmented and thus contribute to social disintegration.

Second, while the safety nets described above are fairly comprehensive in nature, they tend to rely excessively on means-tested social assistance, particularly in the case of high and persisting unemployment or inflation. Evidence from other market economies shows however that excessive reliance on means-tested benefits is frequently responsible for low uptake rates (because of the social stigma involved and the discretionary power of social assistance workers) while generating at the same time strong work disincentives.

Third, while explicit financial coverage for several elements of the safety net (such as unemployment and compensation for food and energy price increases) has been provided in the 1990 and 1991 state budgets, there remain two unresolved problems. Firstly, a number of provisions such as indexation of family benefits or social assistance have not yet received financial coverage in the 1991 budget. Without such coverage, an increase in poverty is likely, particularly if economic reforms are implemented expeditiously. And secondly, the budgetary allocations made for the safety nets have squeezed substantially real public expenditure on health and social security (Table 6.9). While there might be opportunities for savings here and there, the discussion in Section I has stressed the low level of pensions, the irreplaceable nature of many child benefits and the undesirable effects which would follow from a major erosion of such benefits.

Competition for budgetary resources will become even more fierce if unemployment exceeds all forecasts (i.e., 200,000 people by mid-1991 and 400,000 by the end of 1991) and if inflation exceeds the level assumed for the budget projections (i.e., 30%) or estimated for 1991 (i.e., around 70%). In addition to its negative macroeconomic effects, higher inflation would indeed cause a decline in the tax ratio (tax revenue/GDP) and more frequent and higher adjustments of pensions, family allowances and benefits thus draining budgetary resources.

Fourth, the safety nets might also be negatively affected both by social conservatism sprouting from the long term traditions of the country and by unavoidably slow development of those institutions necessary for subduing the impact of the economic changes. Indeed, most of the basic social institutions which ensure the smooth functioning of a market economy are still in the making. These include, among others, mechanisms for collective bargaining, wage and benefit indexation, autonomous social insurance funds, a network of employment offices responsible for active labour market policies and unemployment compensation, public social assistance networks and a private insurance market offering the possibility of additional private social insurance.

Some of this 'institutional underdevelopment' can be made up by private voluntary organisations (with financial support from the state). While the personal assistance and the provision of shelter and food to the very poor and marginal groups such institutions can provide is extremely valuable and efficient, such organisations lack the resources and experience for handling widespread social problems. Their role will therefore always remain ancillary.

Fifth, in the absence of a strong regional policy, the greater emphasis on and devolution of responsibility to local authorities could lead to serious imbalances in the funding and functioning of the safety nets, particularly in poor areas with important ethnic minorities.

In conclusion, while it is unavoidable — and perhaps undesirable — to prevent a fall in the *average* disposable family income, it is likely that the safety nets put into place will not be able to prevent those already living near the absolute poverty line from falling below it. Indeed, these families — which have no financial savings and which cannot reduce further their consumption levels — will not be able to withstand even a modest decline in living standards. For this reason, it is estimated that the number of families living in absolute poverty (currently estimated at 94,000, with 200,000 children, equivalent to 4.5% of all children) may increase three times by late 1991 or early 1992 (HN, 1991).

CHAPTER 7

ECONOMIC REFORMS AND SAFETY NETS IN HUNGARY: LIMITS TO PROTECTION

Mária Zám

Introduction

The underlying assumption of socialist social policy was that the state *cared* about its citizens and ensured their essential security. All social security expenditures were covered by the state from its annual budget in accordance with prevailing political doctrines and economic constraints. Social policy operated in an environment of full employment, almost exclusively work-related social security entitlements, and centrally regulated wages, prices and subsidies. Neither the social security system nor social policy were subject to any form of democratic control. They were thus unable to perceive inarticulate social interests.

As a consequence, the social security system gradually failed to reduce or compensate for the increasing income differentiation which began in the mid-1960s when living standards started to rise. Social policy tended to reinforce emerging social differences and proved unable to respond to new challenges such as poverty, the plight of young families, the elderly on low pensions, housing shortages, underdeveloped regions, or permanent unemployment (Ferge, 1979; Zám, 1990). In spite of these failures, social policy in Hungary did develop, over the last 40 years, a number of social security components which are discussed in the outline below.

I. The existing social security system

This section examines the different components of social security which were built up in Hungary over the past 40 years — in spite of the overall failure of social policy.

1. Subsidies in cash and kind

Subsidies and transfers in cash and kind were extensively used under socialist social policy. It is, however, very important to acknowledge that it was not social policy which was primarily behind the absurd distortions of the socialist price system and the consequent misallocation of resources, but the whole political economy of the one-party state. Nevertheless, it is equally important to understand properly the role which subsidies played in empowering social policy when thinking about the future framework of a social policy which dismisses most of them.

It is almost impossible to assess the contribution of price and producer subsidies to household incomes because they are not well documented and because they had a mutually reinforcing character. However, social transfers in cash and kind, and public expenditure on health, or education, for example, can be assessed more accurately (see Table 7.1).

Table 7.1 *Distribution of the income of households in Hungary according to the source of incomes 1960-1989 (% at current prices)*

Source of Income	1960	1970	1980	1988	1989
Salaries and wages	80.4	76.1	68.0	62.1	58.2
Social transfers in cash (A)	7.0	11.3	18.9	22.4	22.8
Public expenditure (B)	11.4	11.3	13.1	14.4 [1]	15.9 [1]
Total A + B	18.4	22.6	32.0	36.8	38.7
of which:					
pensions	3.7	6.2	12.1	14.1	13.9
health	4.0	3.5	3.9	4.3	N.A.
education, kindergarten	4.3	4.7	5.6	6.6	N.A.

Source: KSH (1990a, p. 26).
Notes: [1] In 1988, personal income taxes and value added taxes were introduced. Therefore social transfers in kind are not completely comparable to earlier years. A) transfer payments to households; B) provisions in kind and expenditures on pensions, health, education, etc.

Between 1960 and 1989, their share in total household income increased from 18.4 to 38.7 per cent. During this period, price-neutral transfers in cash expanded more than three times, whereas other public social expenditures went up by less then 50 per cent. This is perhaps the only impact, suggested by the figures, which may be partially attributed to the economic reform of 1968, although demographic factors such as the aging of the population also contributed to the growth of total expenditure (e.g., on pensions, health, etc.).

Most types of social transfers continued to rise in constant prices during the whole socialist period (see Table 7.2). When they did not grow continuously (crèche, kindergarten, maternity), they often reflected

demographic trends. If the figures are put into per capita perspective within the entitled group, they show even steadier tendencies. Another explanation for certain fluctuations is the lack of automatic indexation. The erosion of certain subsidies (child benefits, child-care allowances) was usually followed by a belated adjustment. The social impact of mounting economic difficulties was reflected in the almost six-fold growth in social assistance between 1980 and 1989.

TABLE 7.2 *Social expenditure in Hungary according to types between 1980-1989 (in billions of forints, 1980 constant value)*

Types	1950	1960	1970	1980	1985	1986	1987	1988	1989
On Services Total (A) of which:	—	22.6	40.9	59.2	69.9	70.8	71.1	72.1	79.9
Health	1.6	6.4	13.0	18.2	20.6	21.4	21.6	21.2	24.3
Crèches	—	—	—	3.9	1.6	1.5	1.6	1.5	1.7
Social items	—	—	—	XX	2.7	2.8	3.0	3.3	2.0
Education	4.0 [1]	7.1	13.0	25.3	24.5	24.5	24.5	26.2	29.4
Kindergartens	0.3 [1]	0.8	1.4	XX	4.4	4.3	4.3	4.1	5.0
Culture/sport	1.1 [1]	1.6	4.4	8.0	10.8	11.1	11.1	11.2	11.1
Amortisation [2]	—	—	—	3.8	2.2	2.1	2.0	1.9	1.7
Other	—	—	—	XX	3.1	3.1	3.1	2.7	4.7
Cash Total (B) of which:	4.3	14.0	34.4	84.4	95.6	101.5	102.7	112.1	119.0
Pensions	2.5	7.7	20.1	56.0	66.2	68.0	69.5	70.8	72.7
Sick leave	0.7	2.8	5.7	8.5	8.4	8.8	8.4	9.1	9.9
Child benefit	0.8	2.4	4.4	13.6	15.4	14.7	14.6	20.1	24.2
Child care [3]	—	—	—	3.9	3.2	3.7	3.8	4.8	5.0
Maternity	0.2	0.1	0.3	1.5	1.2	1.8	1.8	2.0	1.9
Scholarships	—	0.3	0.8	0.1	0.2	1.2	1.1	0.8	0.8
Social assistance	0.1	0.7	3.1	0.8	1.0	3.3	3.5	4.5	4.5
Total (A + B)	—	36.6	75.3	143.6	165.5	172.3	173.8	184.2	198.9
CPI	37.0	59.6	64.1	100.0	138.5	145.9	158.5	183.7	215.2

Source: KSH (1990a, p. 218; 1990b, p. 15) and other KSH Yearbooks.
Notes: [1] 1953; [2] amortisation of publicly owned apartments; [3] child-care allowance and child-care premium; XX included in the figure above.

A breakdown of subsidies in 1989, the last full year of the socialist regime, reveals the areas where social policy may suffer major setbacks if subsidies are removed without compensation (see Table 7.3). The overall amount of subsidies was equal to 50.2 per cent of the otherwise shrinking,

TABLE 7.3 *Social expenditure by type and their ratio to personal income in Hungary in 1989 (current forints and %)*

Type	Total billions	Household forints	Per capita (average)	Personal income (%)
Total services (A)	172.0	44,708	16,678	18.1
of which:				
Education	74.0	19,323	7,175	7.8
Kindergartens	10.7	2,776	1,036	1.1
Primary schools	33.5	8,696	3,244	3.5
Secondary schools	17.7	4,598	1,715	1.9
Higher education	9.3	2,427	905	1.0
Courses, etc.	2.8	736	274	0.3
Health	52.3	13,598	5,073	5.5
Hospitals/clinics	33.0	8,565	3,195	3.5
Ambulatory care	19.4	5,033	1,878	2.0
Others	45.7	11,878	4,431	4.8
Crèches	3.7	952	355	0.4
Social items	4.4	1,154	430	0.5
Holidays	4.9	1,266	472	0.5
Culture/sport	23.9	6,206	2,315	2.5
Canteen meals	5.2	1,352	504	0.6
Amortisation [1]	3.7	948	354	0.4
Subsidies Total (B)	138.6	36,004	13,431	14.6
of which:				
Consumer subsidies	58.6	15,231	3,963	6.2
Rents for housing	8.6	2,235	834	0.9
Heating	20.6	5,353	1,997	2.2
Water utilities in				
— public flats	2.2	559	208	0.2
— private flats	5.8	1,507	562	0.6
Milk	1.6	414	154	0.2
Milk products	2.7	709	264	0.3
Transport	14.1	3,667	1,368	1.5
School books	0.4	96	36	0.0
Theatre	2.7	691	258	0.3
Medical subsidies	15.3	3,963	1,478	1.6
Housing investments	64.7	16,811	6,271	6.8
Mortgages	52.5	13,642	5,089	5.5
Family bonus	12.2	3,168	1,182	1.3
Total (A + B)	310.6	80,713	30,109	32.6

Source: KSH (1990b, p. 15).
Notes: [1] Amortisation of publicly owned rented apartments.

in real terms, of the overall consolidated government budget (see Table 7.10). Hence its restructuring appears inevitable if budget deficits are to be reduced. It is not by chance that, in 1991, the government took a radical step to reduce housing mortgage subsidies since these had already,

by 1989, required more resources than all consumer or health sector subsidies. Crèches, kindergartens, elementary and secondary schools all together received the same amount of subsidies as did house buyers (who kept on paying the preferential 3% mortgage interest rates when inflation soared up to 30% in 1990). Reducing subsidies may affect different social strata very differently (see Table 7.4).

TABLE 7.4 *Ratio of public social expenditure [1] to personal income in the highest and lowest quintile according to family size and the amount of contributions [*] according to family size in Hungary in 1989*

Income groups %	Single persons	Active households couples with				Inactive Total		
		0	1	2	3>	Total households		
		children						
0-5	45.3	45.8	58.1	71.6	82.1	73.7	63.5	71.9
5-10	—	39.8	56.4	55.4	72.0	60.1	50.1	58.2
10-15	27.1	25.2	46.2	50.8	62.9	52.1	50.6	58.2
15-20	20.4	43.8	43.1	48.2	62.5	48.7	44.4	47.9
80-85	—	18.9	29.3	31.7	30.4	24.7	24.3	24.7
85-90	25.6	21.1	29.4	—	20.8	30.3	21.4	28.8
90-95	25.4	18.2	26.4	27.7	22.8	22.1	—	23.7
95-100	22.4	15.0	14.8	22.3	22.9	17.0	18.9	17.1
Total	25.6	20.6	32.6	41.5	57.3	32.7	32.4	32.6
TCbHUF	7.3	54.4	71.6	95.0	31.7	260.0	50.6	310.6
Per HH	41.9	56.9	99.0	136.9	192.2	95.9	44.5	80.7
Per Cap	41.9	24.3	30.8	33.2	35.1	30.6	27.9	30.1

Source: KSH (1990b, p. 22/A).
Notes: [1] Social expenditure on services, subsidies and cash transfers combined; TCbHUF = total contribution in forints/billions; Per HH = contribution per household in forints/thousands; Per Cap = contribution per person in forints/thousands.

For example, families with three children would suffer disproportionately from the withdrawal subsidies without targeted compensation since public social expenditure represents 57.3 per cent of their total per capita personal income, or three times more than that of couples without children. This is even more the case if income levels are also taken into consideration: the poorest families with three or more children are entitled to subsidies equal to 82.1 per cent of their personal incomes.

Public social expenditure thus ensured a certain equalizing balance in society. For people in lower income groups, it represented an irreplaceable flow of income which was vital if they were to meet their basic needs.

Access to education, health and social services, utilities and even housing investment were made possible by these subsidies.

On the other hand, certain subsidies also reinforced social differences inasmuch as they tended to favour people from higher income groups who were over-represented among the beneficiaries. This was notably the case with subsidies for higher education, extension courses, holidays, cultural activities, or housing mortgages.

2. Social insurance

Social insurance became more and more comprehensive and universal in Hungary. Basic health care gradually became free for everyone (see the section on financing) and pensions took into account the peasant farmers who were left out before collectivisation. Retirement age was gradually reduced to 60 for men and 55 for women, first in the state sector and later in co-operative agriculture as well. The number of pensioners made up 80 per cent of the eligible age group in 1970 and more than 100 per cent in 1990 (because of early retirement, disability pensions, etc.). Pensions are set on the basis of the average wage of the person prior to retirement and his/her time in work. They are not indexed to inflation but are occasionally raised. However, most pensions suffered substantially in real value over the past 10 years. Pensions over 3,000 forints in 1980 lost almost a quarter of their purchasing power, and those above 5,000 forints lost more than a third. Only pensions at or under the minimum subsistence level retained their real value (KSH, 1990a, p. 225).

3. Family benefits

In Hungary, family benefits gradually became rather comprehensive, increasingly universal and a less work-dependent form of social assistance. Child benefits were the most important cash benefit and these have lately been extended even to foreign residents and refugees in Hungary. Child benefits are the right of the child and are paid to the parent, guardian or institution until the age of 16 or, in the case of secondary school students, until a maximum of 20 years. In the case of chronically ill children, or children with physical or mental disabilities, there is no age limit. If the income of the handicapped person reaches the level of the minimum pension, the payment of the benefit is suspended. Practically all children receive this benefit, and therefore the number of recipients reflects demographic trends as well as the impact of recent and sizable immigration (mostly refugees). Up to 1990, child benefits increased slightly in real terms according to official statistics (see Table 7.5). In 1990, there was

moderate erosion of the real value of benefits which may continue during 1991 if inflation accelerates and there is no adequate adjustment.

TABLE 7.5 *Child benefit per child according to family size 1987-1991 (in constant 1980 Hungarian forints)*

No. of children	1987	1988	1989	1990	1991 [1]
1 with 2 parents	330	500	610	630	550-640
1 with single parent	520	660	750	740	660-750
2 with 2 parents	520	660	750	740	660-750
2 with single parent	600	740	820	790	740-850
3 or more with 2 parents	600	740	820	790	740-850
3 or more with single parent	600	740	820	790	770-880

Source: Own calculations based on data in KSH (1990a, pp. 15, 239); and *Népszabadság*, 18 January 1991.
Notes: Figures are as of January each year except for 1987 when they are for August. Benefits at current prices were deflated by CPI for the year which does not take into account annual adjustments or rising inflation.
[1] Data for 1991 based on an expected inflation of 22.5-40%.

Child benefits covered an increasing share of the official minimum subsistence level up to 1989 (see Table 7.6). In that year, around one-third of the minimum subsistence level of families was covered by the benefit, and, in the case of large families, more than a half. In 1990, there was a substantial drop in value, especially for large families, which, in the absence of preventive measures, may continue in 1991. The initial value of child benefits in 1991 would cover an unchanged percentage of the

TABLE 7.6 *Child benefits as percentage of minimum subsistence level of families in Hungary 1987-1991 (in % at current prices)*

Type of household	1987	1988	1989	1990 [1]	1991 [2]
1 child with 2 parents	16.7	25.5	31.2	28.4	22.7-26.9
urban	15.2	23.2	29.1	N.A.	N.A.
rural	19.2	29.2	34.7	N.A.	N.A.
1 child with 1 parent	25.9	33.2	37.6	31.7	26.8-30.7
2 children with 2 parents	30.3	38.4	43.1	35.1	29.7-33.9
urban	27.2	34.7	39.3	N.A.	N.A.
rural	34.5	43.9	48.9	N.A.	N.A.
3 children with 2 parents	40.4	48.6	52.9	38.8	34.9-39.9

Source: Own calculations based on KSH (1990a, pp. 224, 239); and *Népszabadság*, 31 January 1991.
Notes: [1] Figures for 1990 are calculated by using December 1990 minimum subsistence level instead of average of 12 months. This bias is partially offset by using the August 1990 benefits instead of January. [2] 1991 is forecast by using an overall CPI estimate in the range of 22.5-40%.

minimum subsistence level of households only if inflation remained under 20 per cent. During the last ten years, there was virtually no change in what the contribution of child benefits contributed to child provision. In 1987, it stood at 18 and 24 per cent for single parent households with 1 or 2 children, respectively, and 20 and 29 per cent for couples with 2 and 3 or more children (KSH, 1990a, p. 225).

Maternity provisions have been also expanding and are rather generous in Hungary (see Table 7.7). This is partially due to a long-standing pro-natalist policy in the country due to decreasing population.

The three-year child-care allowance (fixed monthly allowance), introduced in 1967, was taken up by 60-65 per cent of parents with children between 0-3 years old until the introduction, in 1985, of the more

TABLE 7.7 *Maternity provisions in Hungary in 1990*

Type	Eligibility in months	Amount
1. Maternity leave (pregnancy allowance)	0-6	Full salary (last 20 months average)
2. Child-care allowance (for either parent)	6-36	According to number of children
3. Child-care premium (fathers only after 1 year)	6-24	65-75% of average wage of the person
4. Childbirth grant	at delivery	Lump sum (6,000 forints)
5. Child nursing benefit	0-24	General sick-pay for the whole period
	1-3 years	84 days/child
	3-6 years	42 days/child
	6-10 years	14 days/child
		(Single parents can get more)
6. Mother's-day holiday bonus		1 child - 2 days 2 children - 5 days
7. Breastfeeding time off	6-9	2 hours/day
8. Travel support		90% reduction for families with 3 or more children (under review)
9. Large family bonus		Lump sum for mothers with more than 6 children
10. Home care of disabled children		Minimum wage

Source: Ministry of Welfare, Budapest (1990).

favourable alternative two-year child-care premium (at 65-75% of former wages). The ratio of parents staying at home thanks to the allowance or the premium has risen to almost 80 per cent thus ensuring that the overwhelming majority of young children are taken care of by their parents (KSH, 1990a, p. 18; 1989, p. 21). The amount of the allowance is not automatically adjusted to inflation but is increased annually and usually covers around half of the minimum expenses. The premium is fixed at the average wage of the mother prior to delivery and therefore is not adjusted for inflation, although its minimum amount is fixed every year, usually at the the level of the minimum pension. In January 1991, the minimum premium covered 75 per cent of the minimum subsistence level and was equal to 90 per cent of the minimum wage [2].

4. Child-care institutions

In 1980, almost 15 per cent of children between 0-3 years were taken care of in *crèches*. The introduction of the two-year child-care premium reduced this ratio to 12 per cent. Concomitantly, almost one-fifth of the crèches were closed by 1990. More than half of the closures were the result of companies no longer providing social benefits (GYMF, 1990, p. 45).

In Hungary, *kindergartens* (3-6 years) have a long tradition [3]. By 1988, 86 per cent of children had access to them. Almost all children in kindergartens received subsidized meals. Kindergartens can therefore be considered as almost universal pre-school institutions well integrated into the education system (Nemenyi, 1990). In 1989-90, however, enrolment dipped (to 85.7% in 1989) and enterprises and local authorities started to sell their kindergartens due to financial difficulties.

In elementary schools (6-14 years), *after-class supervision* is provided (as most parents work) and charges are for food only. Between 1970-1989, this service expanded from 18.8 per cent of elementary school children to 39.1 per cent (KSH, 1990a, p. 260). Far more children have access to subsidized school meals.

5. Social assistance for children

There are a few provisions for social assistance for children in need. *Occasional education assistance* is available when parents prove temporarily unable to provide for their child (school meals, clothing, school equipment, after-class supervision fee, etc.) regardless if the parents are responsible for the failure or not. This is an emergency aid to which is supposed to help families to overcome difficult situations. The lowest sum payable in this scheme is half of the child benefit paid to a single parent

with two children. The parents may be asked to account for the use of the aid by the Court of Guardians, but this is neither compulsory nor typical. In 1989, 153,600 families with 348,781 children (12.5% of all children) received this assistance. The average amount paid under this scheme was 40 per cent of the minimum subsistence level.

Regular child-raising assistance is a monthly scheme which has two conditions: per capita family income should be below the minimum pension, and the development of the child would be endangered by the low income of the family. The lowest amount payable under this scheme cannot be less than half of the regular child benefit. In 1989, almost 80,000 children (2.9%) received this assistance and the amount was 15 per cent of the minimum subsistence level.

6. Social assistance for adults

Table 7.8 summarizes the most important forms of social assistance in Hungary (for total costs and historical dynamism see Table 7.2). By far the most common form of social assistance is *occasional or emergency assistance* which may be paid to anyone over 18 years of age whose livelihood is threatened and who cannot expect temporary improvement in their financial position in any other way. The assistance can be paid no more than six times a year, and the amount cannot exceed the upper limit of regular social assistance (i.e., 4,400 forints, or 75% of the minimum subsistence level in 1990)[4]. In 1989, over 420,000 persons, or 5.4 per cent of the adult population of the country, received this assistance on 781,000 occasions. The number of recipients expanded especially rapidly after 1980. In 1970, only 55,600 occasions were recorded; in 1980, 186,000; and in 1985, 485,500. The local governments, which are responsible for this assistance, paid out, in 1989, some 1.51 billion forints, or 0.6 per cent of their overall budget. The corresponding figures for 1990 were 1.7 billion and 0.7 per cent. This was still less than 0.1 per cent of GDP. However, this assistance has been increasing as a proportion of local government spending ever since central and local budgets were separated in 1986 when it was 0.4 per cent (KSH, 1990a, pp. 224, 241).

Regular social assistance is payable to adults who do not dispose of any income, have no relatives to support them and have lost 67 per cent of their capacity to work. Persons totally without income may receive the full amount of assistance (4,400 forints in 1990); others receive an amount which brings their income up to this level. If the recipient has dependents, he or she can apply for a *supplementary assistance*. This assistance remained practically unchanged in real terms during the 1980s, covering 60-65 per cent of minimum subsistence levels. Unlike occasional assistance, the number of regular social assistance recipients declined from

TABLE 7.8 *Social assistance in Hungary in 1989 (provision, number of beneficiaries and % of minimum subsistence level)* *

Provision	Beneficiaries	% of minimum sub [1]
In Cash:		
1. Regular social assistance	47,406	64
2. Occasional social assistance	422,310	(781,122 [2]) 50
3. Fuel subsidy for disabled	33,083	16
4. Personal assistance for the blind	32,000	full board
5. Regular assistance for the blind	1,200	82
6. Financial support for diabetics	30,000	2
7. Family assistance for servicemen	10,000	income supplement
8. Assistance for war invalids	3,850	income supplement
9. Central social aid for Jewish victims of war	150	76
In Kind [3]:		
1. Social feeding	82,606	16
2. Home-care service	82,225	21
3. Elderly clubs	35,709	food charge only
4. Day care for disabled	699	food charge only
5. Family assistance centres	N.A.	free services
6. Institutions - Social Homes	40,322	—
elderly	22,363	33
specialized	7,437	33
mentally handicapped	7,403	24
other	3,119	14

Source: Ministry of Welfare and KSH (1990, pp. 224, 237-41).
Notes: * Total population in 1989: 10.589 million, above 18 years: 7.795 million. [1] In 1989, the official minimum subsistence level was 3,900 forints per person per month ($66). Minimum subsistence level is calculated annually by the Central Statistical Office. This does not include savings for housing. [2] The number of occasions. [3] Charges as percentage of minimum subsistence.

51,361 in 1970 to 47,002 in 1988. In 1989, the number started to grow again and, by 1990, had reached 48,000 (or 0.6% of adults). In 1990, local authorities spent 1.9 billion forints on this scheme, or 0.9 per cent of their total budget which was an increase of 0.2 per cent in comparison with 1986 (KSH, 1990a, pp. 224, 241).

7. FINANCING THE SOCIAL SECURITY SYSTEM

Between 1950 and 1988, social security expenditure and contributions were not in any way linked as, over that period, the social security budget was a mere subdivision of the annual state budget. Salaries were subject to a flat social security contribution rate paid by both the employers and the employees. There was practically no other form of social insurance worth mentioning. Social insurance was separated from the state budget in

1989. This can be seen as the very first step in reforming the social insurance system. Contribution rates were raised to 53 per cent of gross salary (43% by employers and 10% by employees) and, thus separated, the social insurance budget had a surplus both in 1989 and 1990. Child and unemployment benefits continued to be included in the central budget while most social assistance remained with local governments.

In the 1980s, which can be seen both as a decade of crisis and protracted transition in Hungary, public social security, health and education expenditure all together expanded by more than 52 per cent in real terms (see Table 7.9), while the overall budget decreased by 25 per cent on 1980 prices (see Table 7.10). The expansion of social assistance transfers (71%) was particularly rapid. In the meantime, real GDP growth was rather sluggish and the population decreased by more than 3 per cent. As a consequence, the share of social security, health and education expenditures increased both in GDP and the overall government budget. Per capita expenditures increased somewhat even more (see Tables 7.9 and 7.10).

TABLE 7.9 *Social security, health and education expenditures 1980-1991 (in billions of constant 1980 forints and as a % of GDP and NMP)*

	1980	1985	1986	1987	1988	1989	1990 [1]	1991 [2]
In Hungarian forints:								
Health	16.9	19.8	20.4	20.6	23.7	27.6	24.2	26.6
Education	27.8	31.2	31.3	31.3	35.3	41.9	N.A.	N.A.
Social insurance	83.7	94.9	97.4	97.6	117.9	125.2	103.6	101.8
Social assistance	4.2	5.5	5.8	6.	6.3	7.2	N.A.	N.A.
Total	132.6	151.4	154.9	155.5	183.2	201.8	N.A.	N.A.
In % of GDP:								
Health	2.3	2.7	2.7	2.7	3.1	3.5	(3.3)	(4.4)
Education	3.9	4.2	4.2	4.0	4.6	5.3	N.A.	N.A.
Social insurance	11.6	12.7	13.1	12.6	15.4	15.8	(14.2)	(16.8)
Social assistance	0.7	0.7	0.8	0.8	0.8	0.9	N.A.	N.A.
Total	18.4	20.3	20.1	20.1	23.4	25.5	N.A.	N.A.
In % of NMP:								
Total	22.7	24.9	25.6	24.7	29.2	30.7	N.A.	N.A.

Source: KSH (1990a, pp. 15, 54), and Ministry of Welfare, Budapest (1990).
Notes: [1] 1990 not consolidated; [2] 1991 planned figures. () - shares are calculated by using GNP growth estimates and projection for 1990 (−8.2%) and 1991 (−5%) respectively with 22.5% CPI for 1991 (Robinson, 1991, p. 12).

TABLE 7.10 *Consolidated government budget [1] and share of certain sectors in 1980-1989 (in billions of current forints and 1980 prices and shares in % on current prices)*

Main sectors	1980	1985	1986	1987	1988	1989
Budget (current)	368.3	513.5	514.3	578.8	618.3	663.6
Budget (1980)	368.3	370.8	352.5	365.2	336.6	308.4
Distribution:						
Administration	1.8	1.7	1.8	1.8	2.6	3.5
Defence	4.8	7.3	8.0	7.8	9.5	3.5
Economic activities	40.1	44.6	44.6	43.3	40.7	34.8
Health	4.6	5.3	5.8	5.6	7.1	11.1
Education	7.5	8.4	8.9	8.5	10.5	13.6
Social assistance	1.1	1.5	1.7	1.6	1.9	2.3
Social insurance [3]	22.8	25.4	27.7	26.5	35.0	(54.3)

Source: Ministry of Welfare, Budapest (1990).
Notes: [1] Central and local government budget together cleaned from double counting. Budget figures for 1990: current 766.6 bn forints (constant 274.1); for 1991: current 981.6 bn forints (250.7-287.8 with CPI range 22.5-40%).

II. Transition to the market economy and its impact on social policy

1. Economic reforms in Hungary

Hungary has a 20-year history of economic reform. The original idea behind the first major reform in 1968 was a vision of a 'regulated market' which would have left state property — the guarantee of state socialism — intact [6]. It was state ownership and the vested interests of the guardians of state property (managers, ministers, party bureaucrats, trade unionists) which obstructed the full implementation of the reform in the first place and which doomed to failure those elements which were implemented. However, detailed mandatory planning was abolished and a certain flexibility in pricing and investment decisions were introduced. Social policy did not play any significant role either in the conception of the reform or its obstruction. Nevertheless, the emergence and acceptance of the 'second economy', which became both a safety valve in cases where the organized sector had failed and a source of income differentiation, had certain implications for social policy (Gábor, 1979). The lasting legacy of this reform was the cessation of mandatory central planning, a certain decentralisation in regulation and a very limited private accumulation.

After 1979, reforms moved away from the idea of regulated markets and embarked on more institutional initiatives. The so-called 'competitive price system' introduced in 1980 can be seen as the last attempt at reform by price regulation [7] within the socialist framework. Increasingly, the creation of a real market with real market actors and institutions (small

business, commercial banks, monetary policy, financial markets, legal framework, etc.) replaced the issue of regulation and the debate focused on the problem of ownership (Tardos, 1988). These reforms were partly forced on the political leadership by the impending economic crisis (soaring external debt, grave imbalances, the obvious technical and structural obsolescence of the economy, sky-rocketing capital-output ratios, etc.). Debt-servicing and stabilisation became the top priority of economic and political managers who, while trying to remain in control, slowly accepted the idea of ownership reform and the transition to a market economy. The often contrasting requirements of genuine reform aiming at an orderly transition to the market economy and the fire-fighting needs of debt-servicing and stabilisation made it possible, for a while, to conceal the indecision of the ruling political elite. However, it became clear in the growing debate and the subsequent political process that economic reforms could not work in the absence of political reforms, and that a transition to the market economy should be ushered in by the transition to political democracy (Lengyel, 1989).

The establishment of multi-party democracy in 1989 and the sweeping victory of the opposition parties in 1990 accelerated this process and created a conducive environment for the economic transition. The much debated three-year programme of the ruling coalition depicts the most important elements of the transition (*A nemzeti megújhodás programja 1990*), namely, continuing deregulation, anti-monopoly measures and privatisation together with stabilisation. A three- to five-year privatisation process is foreseen by the programme which is likely to be accelerated in 1991 and which will still leave a sizeable public sector when completed. Domestic prices and foreign trade were rapidly liberalized in 1989-90, leaving less than 20 per cent of imported goods under control. By 1992-93, import liberalisation is expected to be almost completely full. The exchange rate was unified by the early 1980s, and thereafter consecutive devaluations brought it closer to realistic levels. In 1989-90, the National Bank pursued a policy of cautious devaluation which is expected to continue in 1991 (real exchange rates altered very little due to inflation). Although this exchange rate policy is under debate and further devaluations are urged, the foreign trade surplus of Hungary was at a record high in 1990. Over the next three years, convertibility of current accounts is foreseen. After years of stop-go measures, the government introduced a programme of subsidy reduction in 1990 which aims at both consumer and producer subsidies. As a consequence, price rises accelerated to 30 per cent in 1990 and may further accelerate in 1991. Interest rates were raised in 1989 and 1990 in line with inflation and were liberalized in 1991. The budget deficit in 1990 was substantially lower than expected.

The resumption of economic growth is expected to occur as a consequence of ownership reform and the deep structural adjustment of the country which entails radical industrial restructuring, massive relocation of resources and people, and a dramatic reorientation of external economic relations with the collapse of the CMEA. The prime target of the government's economic policy is the reduction of the size and the deficit of the government budget "... in order to increase economic efficiency, to eliminate social injustice and ...to curb inflation" (*A nemzeti megújhodás programja 1990*, p. 42). Currently, 60 per cent of GDP is redistributed by the budget and the government wants to reduce this proportion substantially. Already in 1990, fiscal redistribution started to decline. It is planned to fall to 51 per cent of GDP during 1991 and to 46 per cent by 1993[8]. A period of some three to five years is foreseen for the modernisation of public finances which will include the elimination, or radical reduction, of producer and consumer subsidies; further separation of social insurance functions from the government and clearer division between the responsibilities of local and central governments. The government is planning to invest public finances in infrastructure instead.

2. The social impact of the transition

The impact of the transition on people and on social policy will very much depend on how successful the process will be. However, some of the implications can already be assessed.

As the government has made it clear that it plans to keep both its revenue and expenditure below the rate of inflation, those employed in the public sector or left out of the expanding market-sector can definitely expect a certain deterioration in their relative income.

The radical restructuring and tightening of the labour market is causing not only a rapid increase in unemployment but also the loss of income from the 'second economy' which is partly expected to formalize or shrink through intensifying competition for jobs. The removal of producers' subsidies is also contributing to the loss of jobs (in the mining industry in 1991, for example). Formerly, 70 per cent of households obtained some proportion of their income from the 'second economy'. On average, 30 per cent of their total income came from this sector. Those employed in the public sector have been particularly affected because the private sector has been able to offer competitive salaries.

The reduction or removal of consumer subsidies has also hit large sections of the population. Compensation has been only partial, and subsidies and other social expenditure add up about one-third of personal income (see Table 7.1). In 1990, consumption fell and the retail trade, in real terms, contracted by 14-15 per cent. A further 5 per cent decrease in

consumption is planned for 1991[9]. Consumer subsidies may prove to be irreplaceable for those who rely on them for a greater proportion of their income. As mentioned previously, consumer subsidies for the poorest 20 per cent of the population constituted between 48 and 72 per cent of their personal income (and for those with large families, it was 62-82%). For families with two or more children in all income groups, subsidies, on average, represented more than 40 per cent of personal income, while for those with more than three children, the figure rose to 57.3 per cent (see Table 7.4).

Full compensation for subsidy reductions cannot be realistically expected and this will inevitably reduce consumption still further, especially among those who already spend 70 per cent of their income on food alone.

Subsidy reduction has unavoidably fueled inflation. This is due partly to imperfect market mechanisms which have allowed some organisations to offset the loss of producer subsidies by raising prices, and partly because the loss of subsidies to support lower rents and utility charges immediately implied higher prices. In public spending, the government allowed for a 16 per cent increase in inflation when calculating the 1991 budget, although conservative estimates of expected inflation are in the range of 20 to 40 per cent which may well endanger the operation of a number of public services. If, in turn, strict monetary policies are applied to counter inflationary pressures, this may cause more job losses, further recession and a slump in income which could reduce the income of groups at risk to below the poverty line.

As from 1991, local governments will have to rely more on their own resources to ensure a number of services (e.g., education, kindergartens, social assistance, etc.). Some of the services are new, and local authorities will therefore be allowed to raise local taxes and to retain a proportion of personal income tax revenue. Local taxes are new to the public and, as such, they represent a further burden. There is public pressure to avoid or minimize local taxes, but the finances of local governments (especially the slender 16% allocation from central resources) will definitely not permit expenditure without a substantial reduction in services. This is also a highly explosive political issue since most local governments are in opposition hands.

Unemployment as a real social problem only appeared in 1988-89. In 1988, there were only a few thousand people without jobs. In 1989, there were already some 14 to 15,000; by the end of 1990, some 82,000; and in January 1991, a total of 103,278 persons unemployed. Although this latter figure only represented somewhat more than 2 per cent of the labour force, the number is likely to increase to perhaps 10 per cent as restructuring accelerates throughout 1991. In the depressed north-east of the country, those registered as unemployed have risen to 7 per cent and

the estimated total is between 10-12 per cent [10]. Moreover, further increases are foreseen in 1992-1993. Adequate unemployment benefits would be an unwelcome and uncontrollable drain on the budget. It is not by chance, therefore, that in 1991 the Parliament adopted a law which shifted unemployment benefits to a system of insurance. This represents another 0.5 per cent additional burden on wage earners and 1 per cent on employers.

The continuing increase in rents, mortgages and heating costs up to market rates may increase the number of those who fail to pay on time. In 1990, this number jumped three-fold in comparison with the previous year. Preventing a further increase in the number of homeless people (see above) will require a considerable effort by those responsible for social assistance.

The system of social policy and social security, while appearing *over-developed* in terms of funding requirements and redistributional effects at the present level of development of the country, has been unable to manage or mitigate the social problems which arose during the crisis and which are surfacing during the transition to the market economy. It is especially relevant since, unlike the previous regime which tried to buy political stability by social policy provisions, the new democratic government cannot continue funding social policy from borrowed resources.

III. The new model of social policy

There is no blueprint for the reform of social security and social policy in Hungary. Long-term decisions on the overall framework of social policy are being delayed; and, in the short term, trouble-shooting is the only item on the agenda. It is clear that the social security system of the socialist era can no longer be shored up. The uncertainties over the pace and success of economic policies are important variables in determining the practical steps of social security reform. However, a few guiding principles were announced in the government's three-year programme. The government is also working on the preparation of a Social Law (*A nemzeti megújhodás programja*, 1990, p. 119-38).

The government acknowledges, in the name of social solidarity, the right of each citizen to basic security and welfare. It guarantees this by facilitating the establishment and operation of social insurance systems and by providing social assistance to those who are not able to care for themselves, especially the disabled and handicapped.

The government intends to separate social policy from the economy by the establishment of legal frameworks and independent financial resources to meet running costs. More and more elements of social security are shifting towards a system of social insurance (pensions,

health, unemployment benefits, etc.) in line with the new overall economic policies. Pensions, for example, should be guaranteed as a right to all contributors without arbitrary restraint imposed by the balance of the state budget. The separation of the pension fund from the central budget has already been achieved. In the transitory period, the government is assisting in these measures as well as in the setting up of new social insurance funds which should usher in a financially sustainable independence.

Social policy should be fair and meet needs in a democratic way. Social insurance funds and institutions should not only be separated from the budget but should enjoy financial and managerial independence as well.

Social assistance and social policy should have secure, earmarked resources (at least in the form of *pro rata* provision which would determine the share of social policy expenditure) in the central and local government budget. Thus, social assistance would no longer represent the residual element which was the case under the socialist system.

Clear division of responsibilities and functions is needed among the different sectors of social security and between central and local government. The government is also encouraging the entry of new private organisations, churches and non-governmental organisations (NGOs) into the sphere of social policy both in fundraising and in the provision of services.

There is need for rethinking the framework of local social policy in line with the new law on local government. Whereas local governments enjoy wide autonomy in social policy and bear the appropriate responsibility, the central administration should provide adequate supervision in order to ensure the implementation of the new Social Law.

The provision of social services, whenever possible, should be shifted towards market mechanisms in order to increase their efficiency and the use of funds. Whenever public funds are involved, the principles of *sector-neutrality* should be respected (i.e., no discrimination among those who provide social services on the basis of ownership). Privatisation of institutions engaged in social services should be also encouraged.

1. Pensions and health

The first step in separating social insurance from the government budget was already taken by the previous regime in January 1989 when a quasi-independent *Social Insurance Fund* was created to provide for pensions and health care (including sickness benefits and the financing of the whole health service system). The Fund receives a flat-rate social security contribution from both the employers (43%) and employees (10%), and in principle it cannot be diverted to other uses. The state also took responsi-

bility for financing the Fund in case current revenue could not cover expenditure. There are many unresolved problems resulting from the way the Fund was created. For example, its functions were not defined clearly and its scope remained too broad. The same criticism could be made about the forging of health and pensions into a single scheme instead of having a social insurance budget in the state budget. Failure to finance the health system would result in a major drain on the Fund's resources and it would therefore no longer be able to safeguard the rights of the retired to a decent pension. It is envisaged that the Fund will be divided into a pension fund and a separate fund for the health system. The latter will be part of the overall reform of the health sector which has not yet been completed.

The creation of the pension fund underlies the contradiction between the accumulation of contributions during a lifetime and the absence of any accumulated assets in the new fund. This is an especially relevant issue in the light of privatisation and it is foreseen that the new pension fund will be a major recipient of former state property which will help to accumulate assets.

The most important changes in the pension system are likely to increase its flexibility and adjustment to labour market realities. On the one hand, the retirement age (60 for men and 55 for women) is rather low. Therefore, the drain on resources is high and there is pressure to increase the retirement age. On the other hand, demographic factors render it difficult to keep old people in the labour force at a time when an unusually large age-group will be entering a tight labour market in 1991-95 (30-40% more job-seekers than during the 1980s). Also, restructuring requires a more flexible approach to early retirement options. Early retirement was made possible for those within five years of standard retirement age in companies where massive lay-offs were unavoidable on condition that the employers share the burden of paying the pension until the recipient reaches the standard retirement age.

In order to secure the value of pensions in real terms, there are plans to introduce pension ceilings. So far only pensions around or under the minimum subsistence level have kept their real value. The introduction of such a ceiling would limit the commitment of the pension system to a sustainable level and would allow the indexation of all pensions. In 1990, the overall amount paid out on pensions did not change in comparison with 1980 prices (72.4 bn forints) compared to 1989 (72.7 bn forints, see Table 7.2). The planned expenditures in 1991 (262.4 bn current forints) will remain the same in real terms only if inflation does not exceed 25 per cent [11]. If inflation reaches 40 per cent, as expected, then pension provisions will fall by 8 per cent in real terms (67.2 bn 1980 forints).

The government encourages the creation of new private pension

funds not as an alternative but as an addition to mandatory public insurance. This may be especially relevant for high income groups whose needs may not be catered for by a state pension. The same logic applies to the health sector where even more diverse provision systems are likely to emerge (*Programme for the Nations's Renewal: Health Care*, 1990; Jávor, 1990; Gidai, 1991).

2. Unemployment benefits

Unemployment is a serious problem everywhere. But in Hungary it is further aggravated by the fact that the low wage structure instituted under the previous regime allowed no opportunity to save in order to cover the risk of job loss (in much the same way as savings for house purchase were not not taken into account when devising the socialist wage system). Unfortunately, correcting the wage structure can only take place gradually because of the danger of inflation.

One of the last measures enacted by the previous regime was the introduction of an unemployment benefit system in 1989. The source of the benefit, the Employment Fund, was separated from the state budget but it remained within public finances. The scheme provided 365 days of benefits for the unemployed on the condition that they had worked a minimum of 18 months over the previous three-year period, and that the local labour agency was unable to find a suitable job for them. Because of these strict conditions, only 40 to 50 per cent of the registered unemployed could qualify for the benefit. The amount of the benefit represented between 50 and 70 per cent of the former average wage which very often fell below the minimum subsistence level. After the first 365 days, the benefit was reduced by 25 per cent and paid as temporary unemployment allowance for a further 365 days.

In 1991, this system was replaced by an insurance-based scheme to which all employers and employees contribute between 0.5 and 1 per cent of wages respectively. The benefit is paid for up to a maximum of 720 days depending on the length of the contributions and the amount which is related to the previous wage as in the old scheme. The conditions for qualifying for the benefit, however, have been relaxed and people on unemployed benefits are covered by social insurance (health and pension).

Young people without any work experience have been completely left out of the system of unemployment benefits. There are plans to provide these young job-seekers with unemployment assistance for six months at 75 per cent of the current minimum wage which, in early 1991, would have covered about 45 per cent of the minimum subsistence level of a single adult, or 40 per cent of a young family with one child and both parents on assistance.

3. Family policy

There are no major changes planned in the system of family and child benefits, or service provisions (see Tables 7.6 and 7.7). This can be seen as an achievement now that the state is pulling out of a number of other areas. Previous family and child policies are now criticized on the grounds that they contributed to the decline of traditional family values. However, most of the former institutions, benefits and provisions, paradoxically, remain unquestioned. The reason for this is simple to understand: while any further extension of the system is not financially feasible, any cuts would immediately threaten the very subsistence of many families (see Tables 7.1-6). The shortening of maternity leave would increase pressure on the service sector (crèches and kindergartens) as well as on the labour market. There is no real interest in transforming child-care allowances into unemployment benefits. Reducing support would also be unpopular and politically unacceptable to the ruling coalition which is committed to national solidarity and would like to reverse demographic decline.

A more likely danger is that the slow erosion of benefits might accelerate due to under-indexation (see Tables 7.5-6) which would cause a *de facto* reduction and restructuring of the system. Decentralisation of responsibilities for certain service provisions (especially in education) may cause further deterioration if the central government remains uncompromising if local governments fail to finance some of the services in the absence of resources. As noted above, companies are rapidly moving away from social policy and are closing down crèches and kindergartens. Local governments may be tempted, or forced, to succumb to financial pressures as well. If they stop short of closing kindergartens (which was the case in 1990), local governments may not be able to offset the negative consequences of such measures. From 1991 onwards, local governments can charge market prices (or can, at least, cover actual material costs) for school meals. In principle, local governments can assist those families which cannot pay the increased prices but they may not be able to do so if there is further pressure on their social assistance or overall budgets.

Although family policies are likely to remain unchanged for a while, there is already growing debate about the universality of some benefits. Many argue that, given the financial crisis, benefits should be more selective and means-tested. This hardly makes much sense in a situation where average wages are barely more than twice the minimum subsistence level, and families with children are obviously closer to this minimum as benefits never compensate in full for the children. Also, the costs of means-testing should be borne in mind before deciding on this issue.

A more sophisticated argument establishes a link between personal income tax and means-testing. According to this view, child benefits

should be taxed so that better off families would return a higher share of the benefit to the budget than poorer ones. However, this would mean that poor families would also lose part of the benefit and, even if it were raised to compensate the losses, the Hungarian income tax system does not take family size into consideration. However, if properly thought out, this idea could prove useful in restructuring the child benefit system.

4. Social assistance

The responsibility for social assistance is shared between the central and the local governments (see Table 7.8). The central government used to provide the funds, but disbursement and service provision was the responsibility of the local governments. In the new system, local governments, in principle, can offer social assistance freely because they are supposed to be financially independent. However, the central government can neither take unrestricted financial responsibility for the decisions of local governments nor can it pull out from the financing of social assistance as local governments would be unable to take over this function without additional resources. In the new mixed system, the central government transfers a fixed level of assistance to local governments which can use the funds freely for whatever purpose they wish. On the other hand, local governments cannot expect any further support from the central budget for social assistance activities. Social assistance transfers would be increased during the financial year only if child benefits or widows' pensions were to be increased as central social assistance rates are pegged to these benefits. A cynical interpretation, under the present circumstances, might claim that the autonomy of local governments in social assistance would be mainly limited to refusing social assistance because of the yawning gap between needs and financial possibilities.

5. Housing policy

Housing policy could form part of family policy or be treated merely as a part of the subsidy reduction programme, or else come under social assistance measures. In Hungary, however, housing policy cuts across these traditional lines and is one of the most important items in the new social policy.

Various forms of housing subsidies would have required some 106 billion forints, or an unbearable 12.5 per cent of the total planned central budget for 1991, if there were no changes in the system compared with 1990.

Under the new system, public housing will become the property of the local governments along with the whole financial burden of repairs

and maintenance. Local governments can and will sell some of the housing, or operate them at market rates. However, they have to take into account the fact that a number of occupants may not be able to pay the increased rents, buy the property or afford to leave. Rents are expected to increase (after consecutive increases in previous years) by another 100 per cent. Increased revenue from rents may very easily be offset by increased social assistance. Moreover, relocating those who fail to pay or who are unwilling or unable to buy the property is made extremely difficult by the general shortage of social housing.

Assistance to young families who wish to obtain their first flat remains, in principle, unchanged. However, this assistance will also be given as part of the general transfer from the central budget to local governments which are free to use it as they wish. There is no guarantee that local governments will be able or willing to put the same emphasis on this type of assistance which was formerly purpose-designed for young families.

From 1991, new housing mortgages are to be subjected to double indexation. This will be an advantage for new owners as mortgages will reflect not only inflation and interest-rate movements but wage indexes as well. The repayment conditions for loans taken out between 1989-90 at prevailing market rates are to remain unchanged.

The issue of the huge mortgage subsidy which accumulated as a consequence of the fixed 3 per cent interest mortgages taken out prior to 1988, and the soaring inflation rate, was resolved by the Parliament during the last days of 1990. Mortgage owners can choose between two options. They may choose to service half of their debts at market rates (30-36%) and then have the other half written off. The other option is to increase interest rates in 1991 from 3 to 15 per cent for the whole amount with some mechanism to limit the increase in monthly installments. The total estimated saving as a consequence of these measures is some 70 billion forints, more than 60 per cent of projected expenditure if the measures had not been taken and 7 per cent of the total budget. It is clear that this solution tends to favour well-to-do families who are able to repay their already eroded debts with a huge reduction. Poorer families, in turn, are exposed to another substantial increase in their expenditure and remain uncertain as to what the Parliament will decide for 1992. To mitigate any negative effects, local governments are supposed to provide assistance to those who fail to service their increase in mortgage. But, once again, the lack of resources and competing priorities may seriously limit the ability of local governments to help.

IV. The limits to protection

1. Safety net or long-term social policy?

The measures described in the previous sections represent the limits of government action with regard to social security in the foreseeable future. Nevertheless, some original thinking on future social policies continues. A solidarity programme which is being discussed in circles close to the government would aim to prevent large-scale poverty while also defending the middle classes. It foresees the establishment of a *subsistence minimum* which would represent a percentage of minimum wages and guaranteed to everybody. Citizens could apply for this benefit which would be granted on the basis of a means-test. The actual benefit would increase the income of the recipient up to the subsistence minimum.

The programme also plans to build and maintain a certain number of rent-subsidized flats with mixed central and local financing (and open tenders to build them). Tenants of these flats would be party to schemes which would help to motivate them to move on to more self-sustaining solutions.

Introduction of a *food-stamp scheme* is also envisaged by the programme. Families living below the subsistence minimum would be entitled to these food stamps which could be used only to buy Hungarian products in order to support national agriculture [12].

Free medical care would also be provided temporarily and costs would be shared equally by local and central governments. While the programme would entail a number of elements which may be part of a comprehensive social policy reform, it does not provide a framework for such reform. It appears to be more of a safety net designed for an emergency period than a durable long-term strategy. Those parts which are explicitly safety-net elements of the programme are not on the agenda now that the actual transition is underway. There is no justification for linking the more comprehensive and long-term elements to the emergency measures, and then dismiss the whole programme for being unrealistic under the present circumstances.

On the contrary, emergency measures cannot work efficiently without a safety-net framework which is still missing in Hungary. A slightly increased social assistance budget, the opening of soup-kitchens in the major towns and establishing a small emergency fund for providing temporary shelter for the homeless are necessary but not satisfactory measures to face up to the challenge of wide-scale poverty during the transition period.

2. Problems of the new social security system

There is a clear trend in social policy towards more *private involvement* in increasingly insurance-based and multi-channeled social security and service provisions. This is a positive trend in that it fosters a sense of responsibility among individuals and their families. However, there is no strong middle class yet which could provide massive support for such a system. The rich may have the resources to take out private insurance but that alone would not be enough to support a comprehensive market-based social service system. By creating a narrower network of services tailor-made for the rich, social security could be torn apart. Instead of increasing social solidarity, a segregated social security system might contribute to social disintegration.

The *subsidy reduction programme* has very little element of compensation, and even that may have to go to extremely needy cases: one need only cite all those receiving pensions at or below the minimum subsistence level (62%), the long-term unemployed, or those with large families as examples. Meanwhile, people working in the civil service (20% of the labour force) and those dropped from the shrinking second economy may find themselves on the fringe of poverty instead of being part of the middle class who act as a guarantee of stable democracy. As of 1991, there will be no social policy and economic programme to offset the negative impacts of continuing subsidy reduction.

The government has failed to introduce both an *active social policy* and a *comprehensive safety net*. Instead, it has decentralized these functions without providing for adequate resources. It is difficult to judge the real implications of this step at the time of writing (early 1991). However, in the short-term, a crisis in the social security system at local level is easily foreseeable given that central financing increased only by 16 per cent and inflationary expectations are in the range of 35 to 40 per cent. Local taxes cannot prevent the collapse of the system especially in depressed areas where needs are above the national average and taxable incomes are lower. For many local governments, the dilemma will be that of having to choose between closing the local kindergarten or deny social assistance. There is little doubt over which option they would choose. As a consequence, it can be argued that even those elements of the missing safety net which were formally instituted at local level might not be able to function whenever they would be most needed. Any financial impasse might acquire a dimension which could bring the whole new social security system to a point of collapse.

Such economic strictures cast doubts on the ability of the vigorous voluntary and church agencies to cope with the scale of assistance required. Hundreds of non-governmental organisations have sprung up ever

since they were legally allowed to do so. They are already taking care of refugees, the homeless and institutionalised children, etc. However, they are ill-equipped to meet larger-scale challenges and their finances are uncertain. Some rely on piecemeal funding from abroad, some on domestic donations which may dry up as incomes reduce, and some (mostly the churches) can rely on public contributions. It is impossible to predict future social solidarity, but the middle class is currently in grave danger of destruction and the *new rich* who are or will be first generation in Hungary with limited accumulation will hold mostly conservative views on poverty — and peppered with prejudice (e.g., gypsies). Official rhetoric emphasizes individual prosperity, and new solidarity-based trade unions are either missing or are just in the process of being set up.

By far the most prevalent organizations involved in assistance activities are the churches. However, they too have very limited resources. Moreover, they are in the process of reclaiming their formerly nationalized property and are reorganizing their institutions which require extra effort and financing. Part of this transitional financing unavoidably competes with resources and other social needs [13].

The various *social security sectors* (health, social insurance and assistance) are also vying for resources. Ironically, the competition is not only for more funds but also for fewer responsibilities concerning the provision of social services — as if in anticipation of an impending crisis. The impasse between the competing sectors, which all want to retain their former allocations as the only realistic target, makes comprehensive social security reform impossible. This is well reflected by the fact that the 1991 budget has remained unchanged.

The stalemate played an important role in prompting the shifting of unemployment benefits to an insurance basis in early 1991. Leaving unemployment benefits in the social security budget given the expected levels unemployment would have made it impossible to conclude the budget negotiations. The question now is whether the hastily set up unemployment insurance fund will be able to accumulate enough resources before needs rise drastically or whether government intervention will be unavoidable to keep the system going. Without such intervention, unemployment may become unmanageable.

The political parties in Hungary do not differ very much in their social policy. The differences are mainly concerned with the transformation of the economy and on the issue of compensation for former state-owned property. *Reprivatisation of state property* or *large-scale compensation* involves huge sums which the budget did not take into account at all. According to some estimates, it could go up to 100 billion forints, or more than 10 per cent of the total 1991 central and local government budget combined [14]. The implications for social policy could be serious. Despite

divergent rhetoric and unspecified references to a 'social market economy' or 'social safety net', there is a convergence of opinion concerning the independence of social insurance and the need to put it on a proper insurance basis.

The absence of a well-designed safety net and the time-bomb built into the budget suggests that central and local governments will resort to *fire-fighting methods* of social assistance. What would happen if funding were to cease is a source of major uncertainty, even if the social insurance system were to function properly — and, in Hungary, there is no assurance that it will function well during the transition. A number of arguments have pointed out why the previous social insurance system would not work any more and why shifting it to a genuine insurance basis may be difficult, and perhaps even unmanageable. Given these assumptions, families with (many) children and poor households should not expect the new social security system to safeguard completely their already difficult situation. Whole new sectors of society face the prospect of pauperisation — and this will definitely not be prevented by social insurance (which will compound the burden on already over-stretched social services. The lack of adequate protection is evident and calls for immediate measures to install a trouble-shooting safety net. Postponing crucial decisions about wider reform of social policy until better times may indeed prevent their very fulfillment.

NOTES

[1] For more detailed discussion of the debate, see Kornai (1990a; 1990b, pp. 145-55).

[2] *Népszabadság*, 31 January 1991, p. 5.

[3] The first kindergarten, founded in 1828 in Hungary, was among the first in Europe. The first training school for kindergarten teachers opened in 1837. By the end of the 19th century there were already 700 kindergartens in operation. The number of institutions rapidly increased in the 1950s and 1960s, and by 1970 more than half of the children had access to them (Vári, 1989, p. 143-49; Hermann, 1972).

[4] This assistance includes funeral benefits, emergency assistance to victims of natural catastrophes and assistance to prison-leavers.

[5] Social insurance has been estimated by using data from Table 1 which is not completely comparable with Table 3. The present table entails central and local government budgets. It is consolidated but not adjusted for the changes in financing of social security after 1988. In 1989, among other changes, social insurance was taken away from the government budget but, at the same time, some budget items, e.g, health, are financed by the now independent Social Insurance Fund.

[6] The 'regulated market' was not only a Hungarian invention but one which became an enduring though controversial policy objective in Hungary (see Brus, 1972; Kornai, 1990b).

[7] The 'competitive price system' intended to link domestic prices to those of the world market by allowing exporting companies to increase domestic prices as a function of the increase they achieved in the world market.

[8] A new 4-year economic policy package was being prepared in February 1991 by the new finance minister and his team. They plan to achieve stabilisation by 1993. In 1991, a 5 per cent decrease in consumption is planned and 35-38 per cent inflation is projected. GDP will still keep on falling and debts will rise by around 2 billion dollars. In 1992, GDP could grow by 3-4 per cent with still rising debts, stagnating consumption and somewhat decreasing inflation. In 1993, consumption could be increased for the first time and, in 1994, imports could rise again by 6-8 per cent, GDP growth will stabilize, inflation levels could come down to single digits and consumption be increased by 4-5 per cent. This will be the year when the introduction of a comprehensive social safety net becomes a sustainable goal (see Népszabadság, 16 February 1991).

[9] See Gál, 1991, p. 9, and *Népszabadság*, 16 February 1991.

[10] *Népszabadság*, 16 February, 1991, p. 5.

[11] *Heti Világgazdaság*, 19 January 1991, p. 69.

[12] There is increased pressure from agricultural producers for such schemes. Milk producers, during their demonstrations in early 1991, demanded that the government begin a school milk scheme in order to maintain milk consumption which had fallen by 18 per cent since 1988 due to price rises (*Népszabadság*, 1 February 1991).

[13] This can often happen in an indirect way: churches reclaim former property where very often there is already a social institution (e.g., a mother's home or orphanage) which therefore has to be moved somewhere else. The costs of the removal are huge and have to be borne by the social security system. The new church institutions also receive grants from public funds.

[14] *Magyar Nemzet*, 7 February, 1991.

CHAPTER 8

PROMISE OR PERIL? SOCIAL POLICY FOR CHILDREN DURING THE TRANSITION TO THE MARKET ECONOMY IN POLAND

Aleksandra Wiktorow and Piotr Mierzewski

Introduction

As it faces the greatest economic recession of any European country since the Second World War, and as it charts a course ahead of any other central and eastern European country along the untrodden path from totalitarian socialism to democratic capitalism, Poland strives to meet the challenge.

The social and political system is changing: homogenous 'people's masses' are transforming themselves into a pluralist society, democratic institutions are being built or revived, and a market economy is being established. The main task now is to win back full rights for society, and its individual citizens, to encourage personal initiative and to reconstruct a bankrupt economy so as to overcome the "civilization gap" between Poland and western Europe.

This period of transition is certainly a time for great hope and for reconsidering goals and strategies, as well as a historic chance to start anew. However, the transition to the market economy brings with it a number of potential problems, particularly in the distributive field, which may delay or even undermine the success of the overall experiment. First, while it is certain that output will eventually increase, the distribution of these additional resources is likely to benefit some groups much more than others, while 'traditional' and 'new' marginal groups might be left out altogether in this process. Second, the shift of social security to more employment-related and private insurance bases and the slow and uncertain growth of tax revenue might substantially reduce the redistributive role of the state and, possibly, compound the emerging polarization in pre-tax, pre-transfer income distribution. Third, and of most immediate concern, the period of transition to the market economy is being characterized by substantial social costs.

All this may (and certainly can) be avoided if appropriate and cost-efficient policies are introduced and if international support is made available. One-and-a-half years after the introduction of the first economic reforms, however, the social situation has substantially worsened, while distributive and social issues have received little attention so far in the process of Poland's social and economic transformation.

I. Main features and dysfunctions of socialist social policy

1. Articulation of socialist social policy

Despite a number of important differences, social policy in Poland prior to 1989 was built around the same general principles illustrated in greater detail in Chapter 3 of this book. In brief, the system (see Góralska, *et al.*, 1988) was characterized by:

a) Collective ownership (except for agriculture, where three-quarters of output and land was accounted for the private sector, and certain services such as small shops and restaurants) and full employment of all the working-age population. Although hidden unemployment was pervasive, involuntary open unemployment was unknown.

b) Centrally regulated wages and universal social benefits. Unlike most other socialist countries, Poland experienced in the past high rates of open inflation. Wage and benefit indexation was therefore introduced several years ago, although, until 1990, wages were indexed in an *ad hoc* fashion and pay rises differed among sectors, and pensions only began to be indexed in 1985.

c) Generalized consumer subsidies (which represented a substantial burden for the budget) on food, transport, housing and other goods (see Table 8.1).

d) Provision of free or highly subsidised health, education and child-care services. Health care was universally accessible and the professional skills of the health staff were relatively high. Until last year, however, the health system had to deal also with social problems because of the underdevelopment of social assistance. Compulsory education covered all children 6-14 years old, while 97 per cent of children 5-6 years old attended pre-school education. Creches and kindergartens for children 3-5 years old were, by contrast, little developed.

e) Very limited, underfunded and inefficient social assistance services and benefits. The role of social assistance was not recognised for a long time on the belief that socialism had eradicated poverty and other forms of deprivation.

f) An extensive system of social insurance (including old age, invalidity and survivors' pensions, as well as sick-pay benefits, child and family

allowances and a few other minor benefits. Originally social benefits were provided only to those in the state sector by the Social Insurance Fund. Since 1972 also private farmers were granted health insurance, in 1977 pension coverage and, finally, in 1983 also means-tested family benefits (90% of cash benefits to farmers were provided by the state budget). Thus, practically the whole of society, except those who were not employed or self-employed (which in 1989 accounted for less than 0.5% of the total population) was entitled to social insurance.

2. Child and family benefits

Among the various components of social security, child and family benefits were particularly comprehensive. In a sense, all kinds of child- and family-related cash benefits known in the modern world were (and most of them still are) included in the Polish social security system. The main child and family benefits provided were:

a) Maternity leave granted at the rate of 16 weeks on first delivery, 18 weeks on each subsequent delivery and 26 weeks if a woman had more than one child in any given delivery. The maternity allowance was payable at a monthly rate of 100 per cent of the remuneration earned by the mother before the leave.

b) A childbirth grant equivalent to 16 per cent of the average monthly remuneration in the previous quarter was granted to women workers and the unemployed wives of workers.

c) Child-care leave granted for a period of three years, but not beyond the date on which the child reached the age of four, to fathers or mothers with at least six months of employment. The leave could be extended for an additional three years in cases where bringing up a child required special care. However, such leave could not extend beyond the date on which the child reached the age of 18 years. The child care allowance was (and still is) paid for 24 months. In three cases allowance is paid to the end of the leave, namely, to a maximum of 36 months: for children requiring special care, for mothers caring for more than one child born during the same delivery, or for single mothers. The allowance, equal to 25 per cent of the average monthly remuneration (40% for single mothers) in the previous quarter, was means-tested and was paid if the monthly income of the head of the family was lower than 25 per cent of the average monthly remuneration in the previous year. Many families took advantage of the child-care leave, but only a few of them qualified for the allowance since the cut-off income threshold used for means-testing was very low.

The child-care allowance for the care of a healthy child up to eight years old was also granted in the event of an unforeseen closure of the

crèche, kindergarten or school attended by the child.

d) Child-nursing allowance. The mother was entitled to paid leave for caring for a sick child up to 14 years old and a healthy child up to eight years old. The allowance, equal to 100 per cent of the mother's salary, was payable for a maximum of 60 days in any calendar year regardless of the number of children requiring such care. Additional leave was not remunerated. The allowance was granted to the father only in three cases: if the mother was staying outside the place of her residence; if she was unable to provide the care because of sickness or maternity leave; or, if the father brought up the child alone.

e) Child allowance. The history of child allowance in Poland is very complicated. Since 1948 the allowance differed for each successive child in the family. Between 1950-52 and 1970-84 the allowance varied also in relation to the income of the head of the family. However, between 1984 and 1988 the child allowance varied only in relation to the income of the head of the family (there were three, and later five, income thresholds). In 1989 a flat rate, equal for all children, was introduced. Since 1990, the allowance for each child has been equal to 8 per cent of the average remuneration in the previous quarter for each child.

The allowance was granted to all those employed with children up to the age of 16 years or up to the moment of completing schooling (but not beyond the age of 25 years). For children with a disability, the allowance was paid irrespective of age.

f) A means-tested child-support allowance was (and still is) provided to a child living in Poland and entitled to alimony in the case of non-compliance by the responsible parent with an executive court order. Since 1990, the allowance (paid that year to 115,000 children) is no longer means-tested and amounts to 30 per cent of average earnings in the previous quarter.

3. Financing social policy prior to the reform of 1989/90

Government expenditure on consumer subsidies, health, education, social activities (such as sport, culture, etc.) and social insurance benefits for private farm households absorbed a high and growing proportion of the total state budget. This proportion rose from 43 per cent in 1980 to 57 per cent in 1985, while oscillating between 60 and 64 per cent between 1986 and 1988 (Table 8.1). The shares of government expenditure on health (including social assistance) and education (including advanced education) increased substantially between 1985 and 1989. The drop in expenditure on social insurance in 1987 (from 10.4 to 5.1%) was caused by the restructuring of its financing.

TABLE 8.1 *Government expenditure by major categories as a share of total government expenditure*

	1980	1985	1986	1987	1988	1989	1990 [7]	1991 [8]
General admin. [1]	4.2	6.3	6.5	6.7	6.3	6.8	7.6	7.3
Defence	5.8	9.0	8.9	9.4	8.8	7.2	9.1	8.0
Finance	0.2	2.1	0.6	0.3	0.4	4.4	—	—
Science	1.3	0.9	0.6	0.3	0.7	0.4	0.6	0.3
Economic activ.	66.3	45.8	46.0	50.1	50.0	40.4	18.2	12.0
— producer subsid.	44.8	23.4	21.6	20.5	18.8	19.6	5.5	5.6
of which:								
o agriculture	—	2.9	3.7	4.0	3.6	3.2	—	—
o state entr.	—	14.2	11.4	9.1	7.6	10.4	—	—
o various	—	6.3	6.5	7.4	7.6	6.0	—	—
— consumer subsid.	21.5	21.2	24.4	29.6	31.2	20.8	12.7	6.4
of which:								
o foodstuff	14.4	9.0	9.6	11.4	17.2	11.6	—	—
o other goods	0.7	1.8	2.2	2.4	1.3	0.4	—	—
o transport	2.0	2.7	2.8	2.7	2.6	2.0	—	—
o drugs [2]	—	—	0.3	1.0	1.4	0.4	—	—
o housing [3]	4.4	8.4	9.6	12.1	8.7	6.4	—	—
Social insurance [11]	4.6	9.9	10.5	5.1	5.3	8.0	12.1	8.7
Education [4]	7.1	11.7	11.4	12.1	12.0	14.8	14.1	12.7
Health [5]	8.2	11.7	12.0	12.8	13.0	13.6	18.0	20.2
Other social [6]	1.5	2.4	2.2	2.0	2.5	2.8	2.1	1.9
Unallocated [10]	0.0	0.0	0.0	0.0	0.0	0.0	—	—
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Memo Items:								
Gov. exp/NMP	45.1	33.3	32.4	29.7	28.4	25.0	—	—
Gov. exp. in curr. zlotys (tr)	1.14	3.48	4.19	5.03	8.4	29.6	157.6	295.5
Gov. exp. in 1980 zlotys (bn)	1141.7	842.9	851.7	795.3	801.3	818.1	636.0	—
Population (mn)	35.6	37.2	37.5	37.7	37.9	38.1	38.3	38.5

Sources: *Until 1989*: GUS (1987), Tables 2 (147), 4 (224); GUS (1990a), Tables I, 3 (227), 13 (283) and 2 (329); *for 1990* preliminary data from the Ministry of Finance; *for 1991* proposed state budget.

Notes: [1] Includes public security and justice. [2] In 1989, other drug subsidies (about six times as large) were provided by the Social Insurance Fund. [3] Includes capital grants; interest rate subsidies; subsidies for central heating and hot water; maintenance, operating costs and rent subsidies for municipal, cooperative and private housing and a few other minor subsidies. [4] Includes university education. [5] Includes social assistance. [6] Includes culture, art, recreation, sport and tourism. [7] Preliminary. [8] Projected. [9] Calculated using the GDP price deflator. [10] From 1990 a new budget classification was introduced. Data may not be completely comparable with those of previous years. [11] For private farmers only.

This share would be even bigger if the cash benefits for pensions, sick-pay benefits, family allowances and a few other benefits paid to state employees and their families by the Social Insurance Fund (which is managed and accounted for separately from the state budget) were taken into account. Such benefits represented another 14.5 per cent of total government expenditure in 1980, 20 per cent in 1985, and 30 per cent in 1989.

The high priority attached to the social sector in the formulation of national policies is, however, less evident in terms of NMP. Indeed, because of the rapid decline in the ratio of total government expenditure to NMP (which dropped from 45.1% in 1980 to 33.3% in 1985 and to 25% in 1989, mainly because of the massive reduction in producer subsidies — Table 8.1), social expenditure, which includes items such as health, education, other social activities, cash benefits for private farmers and consumer subsidies as well as cash benefits paid to state employees by the Social Insurance Fund declined substantially as a share of NMP over the 1980s (Table 8.2, panel A). The ratio of social expenditure to NMP declined in fact from 26 per cent in 1980, and from 29 per cent in 1981 — when it rose sharply because of the granting of additional benefits to compensate for food price increases (not shown in Table 8.2) — to 22.6 per cent in 1989. This corresponds to a decline of 6 or 7 points of NMP. With the exception of the cash benefits paid by the Social Insurance Fund, all expenditure categories were affected by this decline, particularly since 1985 (Table 8.2, panel A). Such decline is most obvious for consumer subsidies (which dropped from 9.7 to 5.2% of NMP between 1980 and 1989). But it also seems to have affected the health sector and the cash benefit payments from the state budget. The decline in the ratio of social expenditure to NMP is even more worrisome if seen in relation to the gradual worsening of the dependency ratio. Indeed, while the overall population had increased between 1980 and 1989 by only 6.5 per cent (i.e., by about 0.6% a year), the share of dependents had increased from 40.6 to 43 per cent.

The ratio of social expenditure to NMP during the 1980s in Poland differs from that observed in Czechoslovakia and Hungary (see Chapters 6 and 7) and in most OECD countries. If consumer subsidies (which are not generally provided in the latter countries) are omitted, then social expenditure in Poland, which, in 1989, equalled 17.4 per cent of NMP (Table 8.2), appeared to be substantially lower not only than that observed in Sweden (35.1% of GDP), but also of the OECD average (24.6% of GDP) and of Czechoslovakia (24.4% of NMP).

Social insurance benefits, whether paid by the state budget or by the Social Insurance Fund, have represented a relative stable share of NMP

(Table 8.2). Among them, pensions and child and family allowance absorbed the greatest shares (Table 8.3).

TABLE 8.2 *Expenditure on benefits for the population (from state budget and Social Insurance Fund)*

	1980	1985	1987	1989	1990 [4]	1991 [5]
A. *Benefits as share of NMP*						
Benefits in kind	17.3	15.9	16.8	13.0	—	—
Consumer subsidies	9.7	7.3	8.8	5.2	—	—
Education [1]	3.2	3.9	3.6	3.7	—	—
Health [2]	3.7	3.9	3.8	3.4	—	—
Other social [3]	0.7	0.8	0.6	0.7	—	—
Cash benefits	8.7	10.2	10.0	9.6	—	—
From state budget	2.1	3.3	1.5	2.0	—	—
From Social Insurance Fund	6.6	6.9	8.5	7.6	—	—
Total benefits	26.0	26.1	26.8	22.6	—	—
B. *Average benefits per capita/year (in 1980 prices)*						
Benefits in kind	12209	10646	11928	11164	8250	8335
Consumer subsidies	6899	4803	6250	4466	2577	1285
Education [1]	2278	2650	2554	3177	2336	2621
Health [2]	2631	2650	2702	2920	2994	4094
Other social [3]	481	543	422	601	343	335
Cash benefits	6163	6955	7155	7974	7101	—
From state budget	1476	2243	1077	1717	2221	1778
From Social Insurance Fund	4687	4712	6078	6527	4980	—
Total benefits per capita/year	18372	17601	19083	199138	15357	—
Memo Items:						
Average monthly wage (thous. curr. zlotys)	6	20	29	207	1030	1570
Average yearly wage (1980 zlotys)	72480	58027	55368	68527	49841	50330
GDP deflator	100	414	632	3621	24790	37433

Source: Calculated on data of Table 8.1 and on GUS (1990a), Table 1 (334), 2 (194), 3 (227), 8 (232); GUS (1987), Tables 2 (147), 7(152); for the GDP deflator 1980-88 World Bank (1990); for 1989, Kolodko (1991); for 1990, the inflation rate was 584.7% while the expected rate for 1991 is 51%.
Notes: [1] Includes university education. [2] Includes social assistance. [3] Includes culture, art, recreation, sport and tourism. [4] Preliminary. [5] Projected.

Child and family benefits which in the 1980s absorbed between 13 and 24 per cent of total cash benefits to families, and accounted for between 1.1 and 2.3 per cent NMP (see Table 8.3) were, and still are,

meant to provide adequate financial support to families to raise about 11.5 million children and adolescents below 18 years of age, corresponding to about 30 per cent of the total population. Given the low level of average monthly wages (about 1 million zlotys or $110 in 1990, see Table 8.2), child and family benefits constituted an essential component of household income for the great majority of families. This was particularly the case for about 30 per cent of Polish families where the ratio of working adults per child was lower than one, either because these families had more than two children (15% of the families) or because they were single-parent families headed by a single mother or father (respectively 13.7 and 1.7% of total number of families). Around one-third of the Polish families with children, therefore, had unfavourable working adult-children ratios, faced greater risks of poverty and other deprivations and were strongly dependent on child and family cash benefits. In 1990, for

TABLE 8.3 *Social security benefits by main categories (shares)*

	1980	1985	1987	1989	1990	1991
Pension [1]	69.0	67.7	73.5	68.3	71.1	—
Sick pay	15.0	9.2	9.1	5.7	6.3	—
Child and family	13.2	21.1	15.7	24.2	15.9	—
of which:						
Child allowance	6.7	15.4	11.1	21.1	12.4	—
Child-nursing benefit	2.0	1.3	1.0	0.7	0.5	—
Child-care benefit	—	1.3	0.6	0.3	0.9	—
Maternity benefit	2.7	1.7	1.3	0.9	1.0	—
Funeral grant	0.9	0.9	1.4	0.7	1.1	—
Other benefits [2]	0.9	0.5	0.3	0.5	—	—
Unemployment	—	—	—	—	2.0	—
Scholarships [3]	1.5	0.7	0.7	0.9	0.9	—
Social assistance	1.3	1.3	1.0	0.9	3.8	—
Total	100.0	100.0	100.0	100.0	100.0	—
Memo items:						
Total soc. ins. benefits (in current bn zlotys)	214.6	1054.1	1672.5	11152.4	67432.5	—
Total soc. ins. benefits (in 1980 bn zlotys)	214.6	254.8	264.4	308.0	272.0	—
Share of soc. ins. benefits on NMP	8.7	10.2	10.0	9.6	—	—
GDP Deflator [4]	100	414	632	3621	24790	37433

Sources: GUS (1990a), Tables 3 (336), 8 (341), 1 (334), 27 (781); ZUS (1991); GUS (1991); for 1990 data from the Ministry of Labour and Social Welfare.
Notes: [1] Old age, invalidity and survivors', pensions. [2] Mainly birth grants. [3] Only scholarships for university students. [4] For GDP deflator see Table 8.2.

instance, cash benefits accounted for about 10 per cent of family disposable income of a family with two children and two working parents. A low-income single mother with three or more children, in contrast, received family benefits equal to 38 per cent of the average remuneration in the previous quarter, which accounted for between 40 to 50 per cent of her family's disposable income. Despite this relatively important income transfer, one-half of the single mothers could afford only basic food and clothes for their children.

So, while the scope of social policy in Poland was fairly broad, the average government expenditure and benefit provided were not very high. A moderate social expenditure (relative to NMP) was not the only reason. Contributions to the Social Insurance Fund exceeded expenditure through the whole period after the war, excluding the years of strong inflation such as 1982, 1989 and 1990. The surplus, however, was neither deposited in banks nor invested, but was transferred as grants to the state budget. Even the introduction of a new law in 1987 which allowed the deposit of Social Insurance Fund surpluses into a bank did not prevent the state budget from absorbing the surplus as a loan which has been never returned. Therefore, the lack of effective independence of the Social Insurance Fund and the fictitious nature of the Supervisory Board of the Social Insurance Institute were a serious obstacle to the development of an effective social policy.

4. Problems associated with the past approach

The relatively comprehensive coverage of social insurance and the quasi-universal availability of health, education and child-care services ensured progress in health, education and overall welfare, in spite of pronounced economic fluctuations at least up to the early 1970s (Borowczyk, 1986). The infant mortality rate (IMR), for instance, declined from 111 per thousand in 1950 to about 15.9 per thousand in 1989, while visible improvements were also recorded in the field of education. In spite of these encouraging trends, social conditions in Poland improved at a much slower rate than in the countries of western Europe.

Three factors contributed to this slow progress. First, the ideological priority accorded to 'productive activities' ensured that, while most industrial enterprises had surpluses of labour, there was an acute shortage of manpower and other resources in the 'residual' or 'non-productive' service and welfare sectors. In addition, the alleged superiority of state ownership made the development of private welfare services difficult. Second, lack of incentives, poor management and excessive centralization compounded the problems caused by limited funds and personnel. Efficiency and quality of service were never considered as an issue so that

underfunding was often accompanied by wastefulness. Third, in spite of the proclaimed egalitarian distribution of rewards and benefits, substantial differences existed in terms of access to health, education and other services. While party and other members of the *nomenklatura* had privileged access to free drugs, stays at spas and sanatoria, direct access to specialized care, automatic enrolment in the best educational institutions and travel abroad, the majority of the population faced shortages and sundry problems, the most acute of which are briefly illustrated hereafter.

Growing erosion of the real value of benefits in cash and kind

As family and other benefits were broadly linked to average wages — which declined by 20 per cent between 1980 and 1987 (Table 8.2; Kolodko, 1991) — their real value declined gradually during the 1980s. Thus, the erosion in family income, particularly acute in the early 1980s, was aggravated by the decline in the real value of cash benefits. This conclusion is not contradicted by the substantial stability of cash security benefits as a share of NMP and in terms of average cash benefits per capita/year (Table 8.2, panel B), which is largely explained by the extent of coverage.

In addition, average public expenditure per capita in constant 1980 prices dropped substantially for consumer subsidies and health while remaining about the same for education and other social expenditures (sport, culture, etc.) (Table 8.2, panel B).

An underfunded and unsatisfactory health system

While difficulties were evident in almost all spheres of the social services, problems were particularly acute in the health sector. Public expenditure on health was, and still is, inadequate both relative to NMP (3.4% in 1989 as against an average in industrial countries of 6-7%) and in absolute terms ($65 per capita). Only Turkey, at the end of the 1980s, allocated a similar proportion of its GDP (3.5%) to health. In addition, the Polish health care system was, and broadly still is, a state monopoly; in other words, a centralized, bureaucratic, poorly-administered, paternalistic, hospital-centered and under-equipped illegitimate heir of the British National Health Service (see Wlodarczyk and Mierzewski, forthcoming).

Given the poor conditions of the Polish public health services and given the total neglect of health-promotion and environmental protection, it is hardly surprising that the health status of Polish people, and of children in particular, is not satisfactory (see also Chapter 1). Although important improvements were recorded in the 1950s and 1960s, life expectancy at birth has been completely stagnant during the last 10-15

years (for both men and women). Currently life expectancy at birth is about five years lower than the OECD average, mostly because of premature deaths caused by cardiovascular diseases, cancer or accidents among middle-age males (World Bank, 1989). In the 1980s, the IMR declined at much slower rates than in the previous two decades and currently stands at 15.9 per thousand (it would be about 19 per thousand if computed according to WHO norms), as against an average of 7 to 8 per thousand in western Europe. In addition, in Poland, IMR differentials by region, level of education and income remain large, pointing to a degree of social stratification much greater than assumed (Wnuk-Lipinski, 1990; see also Chapter 1). Environmental degradation has also a strong negative effect on child health (particularly in Silesia where, in six of its seven industrial areas, air, soil and water pollution are far above the norm). For instance, in parts of the Silesian town of Bytom, where the concentration of lead, cadmium and zinc in the air are 12 to 46 times higher than the accepted norm, IMR reached 44 per thousand in 1987 (Norska-Borowka, 1989). The incidence of premature birth and low birth weight is also high (8%); while, at school age, 30 per cent of children show some health problems, 15 per cent have somatic development disturbances, 50 per cent have dental caries and 2,200 children are treated for tuberculosis — a disease practically eradicated in most other industrial countries.

Inadequate housing conditions

The centralised distribution of raw materials and limited credit availability paralysed individual housing in the 1980s. State enterprises — which never managed to satisfy the needs in that sphere — performed even less satisfactorily. As a result, the annual number of dwellings built, which averaged about 250,000 per year during the 1975-80 period, declined to about 190,000 in the 1980s (Economic Commission for Europe, 1989). Most families had to wait as many as 20 years to receive a flat from the state. The ensuing forced cohabitation — which implied higher levels of overcrowding for large families — had serious negative consequences on the health status and cognitive and emotional development of children.

A grossly under-developed child-care system

Although it had long been recognised that a child's development requires continuous interaction with his/her peers, kindergarten enrollment in the 3- to 5-year-old age bracket was only 36 per cent, one of the lowest in Europe. The situation was even worse for public creches where only 3 to 4 per cent of children 0-3 years old found places available, generally of

poor quality. Most children were taken care of by their mother on child-care leave (in 28 per cent of the cases), by grandmothers or by (paid) private-care providers.

A 'medicalized' and under-developed social assistance

This service was wholly unequipped to deal with the decline in standards of living and growing impoverishment of large sections of Polish society or with the personal needs of single parents, the handicapped or deprived families. Only in the 1980s — after the percentage of the poor had increased from 9.2 per cent in 1978 to 22.7 per cent in 1987 (Milanovic, 1990) — poverty started to be recognized as a major cause of deprivation requiring policy action. However, the declared intentions of the welfare state were by then confronted with the reality of a relatively poor society.

Growing sense of dependence

Many years of living in a system which imposed a state monopoly in all spheres of life did much damage to the sense of initiative, entrepreneurship and self-reliance of people. With the state as the only employer and provider of services and benefits, the individual, excluded from any responsibility, was both servant and client of the pervasive totalitarian system. Deprived of his/her private initiative and of the right to participate in the decision on how much to tax and how to manage public funds, the individual learned only to demand money from the state. Obedience was the price, benefits the reward, and passivity and cynicism the inevitable outcome.

II. Economic reforms: shock therapy and initial results

Although the Communist leadership had introduced, in early 1989, a number of economic changes (i.e., guarantees of free entry for economic agents, legalization of individual trade in hard currency and liberalization of agricultural prices), it was not until September 1989, when the Solidarity-led government took power, that the drastic reforms of the Economic Transformation Programme were launched simultaneously in the fields of stabilization and structural adjustment.

The main goals of the first phase of the reform (i.e., a 'shock therapy-type' stabilization programme, which lasted from 1 January 1990 until mid-1990) were to stem inflation, reduce the budget deficit to less than 1 per cent of NMP (largely through reduced government spending, particularly for coal and energy subsidies), phase out price controls (with the exception of public transportation, energy and housing rents), contain

further the growth in aggregate demand by freezing wages (through the imposition of a prohibitive tax on wage increases), introduce positive real interest rates and strengthen the national currency (after a significant devaluation in order to make it convertible). Major efforts have been deployed also to obtain a substantial reduction of the total stock of foreign debt (estimated at the end of 1989 at about $41 bn).

Privatization constitutes the second, more structural and longer-term objective of the Economic Transformation Programme. While prior to the reform, private ownership was widespread in agriculture and, to a lesser degree, in trade and transport, a large-scale privatization of industrial enterprises was started in 1990 in order to reduce the role of the state in the manufacturing, energy, mining and construction sectors. While several thousand (mostly small) new companies have already started operating, the transfer of existing public sector firms to the private sector poses many problems. First of all, it requires the revision of more than 100 laws. Second, shortage of indigenous venture capital — aggravated by the lack of a domestic capital market and by the uncertainty about the legal framework regulating ownership, bankruptcy and antitrust norms — and the prudence of foreign capital in acquiring the control of companies of unknown or doubtful profitability has slowed down this process. Small- and medium-size enterprises are the most affected. Third, privatisation is further delayed by the need of simultaneously dismantling existing public monopolies in order to create a competitive environment in which small companies can also operate. Fourth, lack of political consensus about the extent of privatization may delay this process further as highlighted, for instance, by the debate on the restitution of property nationalised during the post-World War II period.

Stabilization and privatization are also being accompanied by major changes in the areas of foreign trade and environmental protection. In spite of the difficulties associated with this task, a large share of Polish trade within CMEA is being and will have to be diverted to other countries. On the other hand, major restructuring, closures and introduction of pollution abatement measures will have to be introduced in heavy industry, construction and mining sectors, particularly in Silesia.

One-and-a-half years after the beginning of the Economic Transformation Programme, a number of achievements, not fully acknowledged by society, have been recorded, namely:

— hyperinflation has been curbed;

— the zloty has become convertible and the dollar has been maintained at a fixed exchange rate;

— queues have disappeared;

— the budget has been balanced;

— privatization has started;

— foreign debt was rescheduled in February 1990, while major debt relief was announced in March 1991.

These achievements have had, however, important negative side-effects. The main criticism is that the reform has 'overshot' its targets. Industrial production declined in 1990 by 25 per cent instead of the predicted 5 per cent; GDP fell by 18 per cent instead of the targeted 3.1 per cent; at the end of 1990, the unemployment rate reached 8.1 per cent instead of the 2 to 3 per cent assumed; the trade balance recorded in 1990 a surplus of $4.4 billion instead of a projected deficit of $0.8 billion. These figures suggest a case of 'overkill' or 'overstabilization' with all its inherent problems of under-utilisation of resources, excessive contraction of investment, social costs, etc. In addition, while hyperinflation was curbed, prices have continued rising in the second half of 1990 at 4 to 5 per cent monthly, while in January 1991 inflation accelerated to 12.7 per cent a month. And, finally, for the reasons discussed above, the pace of privatisation has been very slow. In particular, the hopes for a fast development of the small private sector have not materialised. While private commerce, mainly street commerce, has developed, only a small number of new manufacturers requiring substantial new investments have been created.

The drastic lowering in standards of living associated with the economic reforms of the last 18 months has already caused considerable political turmoil. The establishment of the first non-communist government in September 1989 had raised great expectations for rapid improvements in the standard of living. As soon as it became clear that improvements could not be achieved in the short term, public dissatisfaction became apparent. In the middle of 1990, railway and public transport workers and miners went on strike demanding higher wages. Dissatisfied with the government's agricultural policy and confronted with free market mechanisms, farmers also protested. The atmosphere of social discontent grew tense during the presidential campaign. All candidates, excluding the then Prime Minister, Tadeusz Mazowiecki, severely criticized the economic and social policy of the government, recommending faster privatisation and improvements in standard of living and social services. However, while the presidential campaign fueled often impossible revindications, the economic policy of the Mazowiecki government has been continued by the new government with only slight modifications.

III. Social conditions during the transition

A precise assessment of the social impact of the Economic Transformation Programme is, for the time being, somewhat premature. A more thorough evaluation will be possible only after completing the analysis of the 1990

household budget survey and of other data on living conditions. Even at this stage it is evident, however, that for most people the alleged economic successes have been overshadowed by the hardships of everyday life and, in particular, by the increase in poverty which, according to the household budget survey, affected, during the first three quarters of 1990, 40 per cent of the total population (GUS, 1990b). The erosion of the economic resources of families was much greater than expected. During the first nine months of 1990, household income declined by 27 per cent, while the value of savings fell fourfold. In addition, registered unemployment — unknown in post-war Poland — had affected 1.1 million people, or about 8 per cent of the working population in December 1990 (GUS, 1990b). The worst situation is in small towns and for young people, particularly high school and university graduates. The increase in food prices was also painful. In spite of the stockpiling of food (and other goods) prior to price liberalisation of 1990, the share of food expenditure exceeded 50 per cent of total family expenditure in families with employed breadwinners and 60 per cent in families of pensioners (GUS, 1990b; GUS, 1991). The consumption of all kinds of food (including milk and milk products) has fallen except for meat, whose consumption increased slightly after rationing was removed. Although no firm conclusions can be drawn because of the lack of precise data on food intake and nutritional surveillance, it seems that the nutritional status of children of disadvantaged families could have been negatively affected by the economic crisis, especially by the withdrawal of milk and other food subsidies. There have even been a few scattered reports of children losing consciousness at school because of hunger. At present only 58 per cent of children in rural areas and 92 per cent in towns have three meals daily, while 25 per cent of school-age children do not eat breakfast and 80 per cent do not drink a glass of milk daily. There is also evidence that with the withdrawal of subsidies, charges for rent, electricity and gas increased substantially and many families fell into arrears with payments.

In response to this deteriorating situation, at the beginning of 1990, the Ministry of Labour and Social Welfare organised soup-kitchens and overnight shelters for the poor, but the latter are insufficient.

The economic crisis has also affected the functioning of social services because of cuts in public expenditure. Although parents only have to pay for food in state-financed nurseries and kindergartens, the rise in the cost of school meals due to the liberalisation of food prices and to the abolition of school meal subsidies has forced many families to withdraw the child from these institutions and to look for other forms of care. In 1990, the monthly cost of kindergarten meals per child was equivalent to about 15 per cent of an average salary. In addition, as part of the reform, crèches and kindergartens were transferred to local government adminis-

tration. However, because of the shortage of funds affecting most local governments, fees were increased and enrolment declined. For the first time in many years, there are now free places in child-care institutions, while many of them are being closed or changing function.

Over the last years, 40 per cent of children had spent their vacation in publicly supported summer camps. Their number decreased dramatically in 1990 as local governments and companies reduced subsidies to summer camp projects. This could jeopardise the health of children, particularly in areas affected by ecological degradation.

The access to education and culture has also become much more restricted following the liberalisation of the price of paper and the withdrawal of subsidies on school books and teaching aids. Prices of books, including textbooks, have risen disproportionately and many families cannot afford to buy them. For instance, the yearly cost of textbooks for a child in primary education equalled, in 1990, one month's average salary. Also, many cultural institutions, including local libraries, were closed down. Local governments are expected to assume greater responsibility for such institutions, but their action is constrained by lack of resources.

The single most severe problem in this process is that while such deterioration in living standards affects the majority of the Polish population, families with many children (about one-fifth of the total) and pensioners face the most serious deprivations. In particular, children in families with high dependency ratios, with parents with low education or engaged in low-paying jobs, or affected by other risk factors (single parenthood, handicapped, alcoholic parents) face a very real possibility of poverty, worsening health, poor nutrition and greater social marginalisation. Ironically, these families — which faced the greatest risk of poverty and social deprivation under the previous regime, and which, therefore, had the greatest hopes for improvement — are those most affected during the transition to the market economy.

IV. The new model of social policy

1. Political considerations

Overall, social policy has remained a marginal topic in the debate about the political and economic transformation of Polish society. Despite national and international pressures, little emphasis and few resources have been placed on the introduction of adequate safety nets, while the establishment of a new model of social policy seems to remain a long-term task. Two factors have possibly contributed to this situation. First, the old dogmas about 'productive' and 'non-productive' sectors and the

negligence of the human capital factor have been compounded by the neophyte faith in neo-liberal economics and by a popular backlash against state intervention in any sphere of life. 'Socialist' is a discredited word. Therefore, 'social' is also suspect, while 'public' sounds dubious. Second, in a situation of rapid deterioration in standards of living, emphasis was placed on economic and immediate relief measures.

The transition from 'real socialism' to 'real prices' is therefore a painful one. A strong social safety net is therefore needed to ensure acceptance of the economic and political reforms. Is the present political destabilization a cause or an effect of the Economic Transformation Programme (often referred to as the Balcerowicz Plan)?

2. Factors influencing the choice of the new model of social policy

The main architects of the transition to the market economy are economists with only a modest knowledge of social policy, favouring a limited state intervention in the social welfare sphere (as in the case of Chile) and overlooking the experience of most OECD countries where economic efficiency is the result of heavy investments in human capital and of a political consensus based on a well-developed system of social guarantees.

The Balcerowicz Plan introduced on 1 January 1990, in particular, did not acknowledge the importance of an appropriate social policy and broadly ignored its social impact. This is one of the reasons why this led to its rejection by voters during the presidential elections. The new government must now promptly formulate and make public an outline of new social policy. Unfortunately, agreement on the new policy has not yet been reached.

Of the three hypothetical models of social policy illustrated in Chapter 2, the politicians with influence on economic decisions favour the *modern liberal model*, such as the United States model, while social politicians are advocates of the *modern conservative model*, such as the German model (on this point, as well as on the more general issue of the welfare state in Poland, see Rajewski and Rutkowski, 1990). The *social democratic model*, from Sweden, is rejected by both groups because it would be difficult to implement in Poland. For the foreseeable future, Poland will not be in any condition to generate the considerable amount of tax revenue needed for its functioning, as the new tax reform will be introduced only in 1992 and will likely develop in steps. Nevertheless, the introduction of direct income tax will have positive effects for social policy, as it will help people to understand that social benefits and services are financed by society itself, and that the introduction of new benefits or services, or improvements in their quality, cannot be achieved without either higher taxes or changes in spending priorities.

The United States model of social policy has no chance in Poland. The cancellation of many of the existing cash benefits (e.g., child allowances or sickness benefits) seems to be impossible, as individual insurance of such risks will not be possible for most people for at least one generation given the present low level of income and savings and of their expected slow increase. In addition, it is likely that future savings, particularly of young employees, will be used to purchase new houses as the present destitute credit system forces people to buy with cash, while the reduction of housing subsidies and the shortage of flats have inflated tremendously their prices.

The German model seems to be the easiest to implement and requires the smallest changes. Decisions on the proper balance between state involvement and individual contributions can be made on the basis of a new social contract. It will be necessary, however, to depart from the present range of service, if the level of standard payments and the rules for their financing are adjusted to the new conditions of the economy. At the same time, the modern conservative model would require attributing a greater role to complementary private insurance and improving substantially social assistance (Institute for Economic Policy and Research, Karlsruhe, and Centre for Statistical and Economic Analysis, Warsaw, 1990).

3. Reforming the old elements of social policy and creating new ones

Under the pressure of economic change, modifications of Polish social policy have already been introduced and include the automatic indexation of wages, new laws on employment and social assistance and an amendment to the pension law. In addition, some family benefits have gained legal status and the government is working on the reform of health care. Private schools can now be freely established with the financial help of parents, social organizations, foundations and the state. The new model of social policy, therefore, includes both universal and selective benefits and services, while aiming at unifying the Social Insurance for all the groups (excluding private farmers, 90% of whose benefits will continue to be financed by the state budget). Among the salient features of the reformed system are the following:

— In 1990, *automatic indexation* replaced the *ad hoc* indexation prevailing under the communist regime. The new indexation, however, is below the inflation rate due to the necessity of curbing hyperinflation. Between January and April 1990, wage increases covered only 20 per cent of price increases; in May and June, 30 per cent; in July, 100 per cent and during the rest of 1990, 60 per cent.

— The new employment law has introduced *unemployment benefits* amounting to 70 per cent of the previous remuneration up to the first

three months of unemployment, to 50 per cent during the next six months and up to 40 per cent for a further three months. The unemployment benefit cannot be lower than 95 per cent of the minimum monthly remuneration or higher than the average monthly remuneration. Rights to a higher rate of benefits is given to unemployed persons undergoing vocational training and to persons five years away from retirement. A budgetary allocation of 1,349 billion zlotys (equal to 0.8% of total government expenditure and representing 2% of total cash benefits paid in that year) was made on the assumption that unemployment would not exceed, in 1990, 400,000 people (see Table 8.3). The law still requires some improvements in the area of active employment policies.

— The new law on *social assistance* (which replaces the old one passed in 1923) aims to transfer this task to an efficient public sector institution which would comprise the central and the local governments, the church and private agencies. Social assistance, which will provide means-tested benefits and personal support to those in need, is meant to deal with the economic and social problems induced by the transition to the market economy as well as with those deprivations neglected during the communist rule, such as loneliness, disability, homelessness, alcohol and drug addition, unemployment, orphanhood, life ineptitude, etc. A budgetary allocation of 2,580 billion zloty was made in 1990 (equal to 1.8% of government expenditure and 3.8% of total cash benefits, see Table 8.3), while the number of staff in charge of casework and of administering the means-tested benefits is being increased (Szumlicz, 1990 and 1991).

— The reform of *local governments* introduced decentralization of social policy. Local authorities are responsible, and will be even more so in the future (Table 8.4), for health care, education, culture and social

TABLE 8.4 *Shares of central and local government expenditure allocated to the social sector*

	1980	1985	1986	1987	1988	1989
	A. *Central government*					
Education [1]	2.3	3.5	3.5	3.8	4.2	4.7
Health [2]	1.3	4.7	5.2	5.5	5.1	4.4
Culture and art	0.6	2.3	2.1	2.4	2.5	2.9
Recreation, sport, tourism	0.2	0.3	0.2	0.2	0.2	0.2
	B. *Local government*					
Education [1]	28.0	32.1	31.0	30.0	30.1	36.1
Health [2]	38.4	28.9	29.6	29.6	31.2	33.2
Culture and art	3.1	0.3	0.5	0.4	0.6	0.7
Recreation, sport, tourism	1.1	1.1	1.2	1.2	1.6	1.7

Source: GUS (1984), Table 8; GUS (1990a), Table 9.
Notes: [1] Includes university education. [2] Includes social assistance.

assistance in their areas. The state budget will support the weaker local budgets because self-financing capacity varies substantially across regions. As the ability of local authorities to generate additional revenue is limited, an important role will be played by non-governmental institutions which help various groups of people in need and which are financed with their own means and supported by the state.

— The *amendment of the pension law* recast the system of pensions. However, under conditions of hyperinflation, the prevailing method of partial ex-post indexation prevailing led to massive losses of purchasing power for most pensioners. This in turn made additional payments necessary during 1990.

The new regulation introduced a three-monthly indexation of pensions according to the formula:

$$R_n = P_n\text{-}1 \times W_n/W_n\text{-}1 \times S$$

where:

R_n – the rate of pension in quarter n {n = 1, 2, ...}
P_n-1 – the basis of calculation of pension in quarter n
W_n – anticipated average monthly remuneration in quarter n
W_n-1 – anticipated average monthly remuneration in quarter n-1
S – relation of first time accounted pension to its base of calculation, $S = R1/P1 \times 100$.

Pensions are indexed in the last month of each quarter with compensation from the first month of the quarter. The law also foresees wage indexation which is the base for calculation of pensions.

— The reform will also cover the *financing of social policy*, particularly the financing of the Social Insurance Fund. It is suggested to split the contribution (so far paid only by the employer) between the employee and the employer. This, however, will require an increase in wages so as not to depress the employee's purchasing power. Moreover, it seems necessary to divide the Social Insurance Fund into pension fund, sickness (including maternity) insurance fund, and accidents at work and occupational diseases insurance fund, to facilitate the calculation of contributions and benefits and improve the efficiency of insurance.

The financing of sickness benefits is planned to be transferred partially — after a few days of sickness — to the Social Insurance Fund where part of the expenses will be covered from contributions (until now, the state sector employees were covered 100% by the employer from the payroll).

The transfer of the financing of family allowances to the state budget is also being considered. The state budget would gain from additional

resources from the employer's savings on sickness benefits, although this would not cover the increased expenditure of the state.

4. Health-care reform: a fundamental transformation

Patients have, quite simply, lost patience. Health care reform is now one of the decisions most awaited for by the general public and the medical profession. There is an urgent need to replace paternalism with professional autonomy, rationing with freedom of choice, state with community and individual responsibility, cure with care, privileges with entitlements, administration with management, and to match equity (proclaimed but never attained) with efficiency. In this process, it is necessary, however, to avoid commercializing or privatizing the health system, shifting costs to patients and replacing a good Samaritan ideal for a business-like medical one.

The government has accepted reform proposals and introduced a comprehensive employment-related health insurance system based on strong primary care (family doctors), self-governing hospitals, decentralization with local community involvement, consumer participation, health promotion and prevention. The system will aim at guaranteeing adequate quality of service, while patients' rights will be legally stated and professional managers will replace the present physician-based administration (Wlodarczyk and Mierzewski, forthcoming).

While the state guarantees equal and universal access to health care, a number of unresolved issues remain. These concern access for those not covered by the compulsory health insurance or by supplementary private insurance, cost containment in the public sector, and the overall underfinancing of health care which — during this difficult period of economic and social reforms — is becoming even more acute (Table 8.2; see also World Bank, 1989). Despite these problems, a major improvement in services is expected as a result of the separation of financing and provision. In this way, the state monopoly should be broken down by introducing 'managed competition' among various providers of care on the supply side. The 'public funding, private provision' option will be possible. The freedom of choice of family doctors introduces competition on the demand side.

While none of these changes affect the essential entitlements of the population to health care, the established privileges of the former *nomenklatura* will be removed. A new 'social contract' should be agreed upon, redefining the guaranteed scope of services and stressing the role of individual responsibility.

To achieve the reform's objectives, it is necessary to attain a public awareness that an efficient health care necessitates a shift from curative

medicine to health promotion and prevention, hospital care to ambulatory care, institutionalized to home and community care, highly specialized care to that of general practitioner, and traditional disability benefits to social and professional rehabilitation.

V. Changes in child and family policy

As previously mentioned, child and family policy and benefits were fairly comprehensive and remained broadly unchanged except for the modification in the method of calculation introduced in 1990. No important changes are expected in the short run, and child and family benefits are likely to remain the same as those discussed in Section I, except for the relatively minor amendments illustrated below. In the long run, however, changes in the child and child-care allowances will be inevitable.

1. Changes in the area of child and family policy

— The new project of *maternity and sickness insurance* does not introduce any changes in regulation of maternity leave and allowance. No changes are expected either for the *child support (alimony) benefit*. The same applies to the *childbirth grant*. A different method of calculation is proposed, but the amount of the benefit will remain the same. However, as its value is very low (it does not even cover the cost of the layette), the birth grant ought, in the future, to be increased substantially.

— The future of the *child-care allowance* is, by contrast, controversial (Ministerstwo Pracy i Polityki Spoleczne, 1990). The liberal economists favour its abolition, while those in favour of it would like to extend it to all women on maternity leave. The situation is more complicated in a period of very high unemployment and budgetary restrictions. The same problem is under discussion and a new solution must be found, though complete abolition of this allowance does not seem possible.

— Two changes concerning the *child-nursing allowance* are included in the new draft regulations, namely, a reduction of the rate of the allowance to 80 per cent of remuneration (i.e., to the level of sickness allowance for workers) and the entitlement of the father to the care allowance.

— The revision of the *child allowance* is in progress, although any fundamental change is unlikely. The revision is considering whether the family allowances should be retained in the Social Insurance Fund or whether its coverage should be extended or transferred to the state budget. In Poland, only artists (painters, sculptors, writers, etc.) do not qualify for family allowances, while for independent farmers the allowance is subject to means-testing. One proposal has been made to

extend the allowance to the categories at present excluded and to transfer its financing to the state budget. According to an alternative proposal, the child allowance should be abolished altogether and replaced by means-tested benefits for poor families.

A change in the method of calculation of the child allowance does not seem possible until the rise in the cost of living is stopped. In future, the child allowance will likely become universal, but their value will be lower in order to offer more to the poorest families. The option to completely abolish the child allowances is not popular among social politicians nor among society.

2. Monitoring the welfare of the family

Until now, the identification of families in poverty was difficult, as statistical research limited itself to the occasional analysis of household budgets and to the examination of the living standards of only a few selected types of families. Traditionally, families with a current income below the so-called 'social minimum' were considered poor (Góralska, 1986). This category, however, cannot be regarded as constituting a real absolute poverty line, as throughout the whole post-war period the nutritional standard used for calculating the social minimum was higher than real average food consumption. This bias quite clearly needs to be corrected. On the other hand, other costs have increased inordinately as a result of the Economic Transformation Programme. For instance, if a family now has to rent an apartment, not even a high income can ensure an acceptable standard of living, as the rental of a small apartment exceeds the monthly average wage.

A new method of calculating the poverty line is also necessary for the granting of social assistance benefits. According to the new social assistance act, social workers should identify the families in poverty in their area. Social workers, however, are not yet well prepared to undertake this task and other duties for several reasons. There were too few of them (8,000 for 2,000 districts throughout the whole country in 1989). Their remuneration was very low and it was therefore difficult to find a person willing to work in social assistance for any long period of time.

The new social assistance act attaches a high priority to needs monitoring. Social workers are obliged to identify the families' standard of living and social circumstances on the basis of individual examination. They should evaluate the scale of social threats, and propose forms of cooperation and support for people covered by social assistance. An increase in the number of social workers is foreseen, as well as a substantial rise in their remuneration and the possibility of in-service training.

VI. Safety nets: immediate measures being implemented for the poor

The deep economic recession has brought severe social problems into focus, including a substantial increase in the number of people living in poverty (particularly old people, disabled, widows living on pensions and bringing up children, large families, single-parent families and families of the unemployed). Safety nets have been put into place by the government to reduce the spread of poverty and of the deprivations associated with it. Among the main measures introduced are:

a) Soup-kitchens and overnight shelters for the poor (opened at the beginning of 1990 by the Ministry of Labour and Social Welfare);

b) Budgetary allocations for unemployment compensation and additional social assistance benefits (equal to about 0.5% of NMP);

c) Private charities and local level institutions (which have been encouraged to intervene in support of the poor).

Unemployment is expected to remain high for a long time and even to increase. As unemployment benefits are paid for a duration of up to only one year, the number of families deprived of part or all labour income is also expected to increase. At the same time, the erosion of social insurance benefits which occurred over the last two years is not likely to be compensated and may even continue if inflation is not brought completely under control. Social assistance is therefore expected to be the main 'safety net', particularly after the enactment of the new law which introduces a series of means-tested benefits targeted at the poorest. These include:

— A permanent allowance for persons without means of subsistence and unable to work (because of invalidity or old age), and persons not working or leaving a job to bring up disabled children demanding permanent care. The amount of the allowance is 90 per cent of minimum old age pension (i.e., 31.5% of average remuneration, or roughly $35). A supplement accounting for 10.5 per cent of average remuneration can be added for chronically sick persons, pregnant women, total invalids and persons above the age of 75.

— A temporary allowance for persons whose means do not provide for their and their dependents' basic needs if the household income per head is not higher than 35 per cent of average remuneration and, additionally, one of the following circumstances appears: chronic disease, lack of employment possibilities, disability, or lack of eligibility for survivor's benefit. The amount of this allowance is the same as the permanent allowance and its duration is determined on the district (or *gmina*) level.

— A lump sum allowance for urgent needs (e.g., apartment repairs, coal, clothing).

— An allowance for persons whose housing expenditures exceed

8 per cent of their monthly income, providing that the living space is not more than 35 m² for a one-person household and 70 m² in a household of six persons or more. It is awarded individually and covers the portion of housing expenditures which exceed 8 per cent of the family income. Additional allowances may be granted for electricity, central heating (or coal-firing) and gas payments. About 30 per cent of the families are estimated to be eligible for this allowance.

— A care service for persons who need others' help in everyday life. This may be free, if family income per head does not exceed 35 per cent of average remuneration.

— A stay in a social assistance home for persons who cannot be provided with care services at their place of residence. The payment accounts for 200 per cent of the minimum old-age pension (70% of average remuneration), but not more than 70 per cent of the person's income.

— Coverage of health expenditure for persons not eligible for medical insurance and who do not have adequate financial means.

— Support to deal with official matters (environment, law) and psychological counseling.

— Family or individual help to become self-sufficient, support in kind (e.g., machines, equipment) or in cash (repayable or part rebate).

— Providing shelter, meals and clothes to persons in need.

The list of benefits is not complete. Families can also receive means-tested cash assistance for other purposes, such as to cover the cost of nursery school or kindergarten.

Social assistance is organized by the government and self-government administrations cooperating in this area, with social and religious organizations, foundations and individual persons. The district (or *gmina*) social assistance centers are responsible for identifying needs and giving support to all who need it. The social assistance centres operating at county level (or *voivod*) prepare the balance of needs and resources, deal with social workers, training, and support the activities of voluntary organizations.

Despite these laudable efforts, it is evident that the safety nets in Poland were developed 'too little', and 'too late' and that, in 1990 at least, they were unable to prevent a substantial increase in poverty and in the social dislocations described in Section III. While there are indications that the total amount of public resources for unemployment and social assistance will rise in 1991, these resources remain inadequate in relation to the size of the problem while their increase is expected to squeeze the real value of other social benefits or services. Greater resources ought to be, and could be, made available, particularly in view of the large reduction in public expenditure on consumer and producer subsidies in the 1990 and 1991 budget. In addition, the ability of such a

safety net to alleviate poverty will be much reduced by the relatively under-developed state of the social assistance administration. It is also important to bear in mind the 'social stigma' associated with applying for financial help (particularly in Poland where there is no such tradition) and the high degree of discretionality associated with means-testing, which will likely reduce uptake rates among the poor.

VII. Towards an uncertain future

Poland has entered the critical stage of its structural adjustment efforts. 'Shortageflation' (the inheritance of the past) could transform itself into 'slumpflation' (a possible feature). Political destabilization could jeopardize economic reforms. The reverse could also apply: the failure of economic stabilization could destabilize the political forum.

The economic transformations in Poland also result in the changing of social stratification. The number of self-employed people will increase. They will have to be self-reliant and not depend on the government. The middle class will emerge as a principal beneficiary of the reforms, replacing the traditional "intelligentsia". However, the employees of big state-owned companies will continue to be the majority of the working population. They were the first to take up the fight against the Communist system inside the Solidarity movement; now they are the first to bear the burden of crisis.

With NMP still below its 1979 level, there is no improvement in living standards expected in the very near future. The principal concern is to protect the present standard of living. Even this modest objective will not be easy to achieve, however. Indeed, the state budget in 1991 foresees the elimination of practically all remaining consumer subsidies on goods and services, while a substantial rise in housing costs, energy and communication is expected. In addition, a value-added tax will be introduced for the first time in 1991, and the extremely unpopular restrictions on wage increases will be retained in the public sector. A current wave of strikes in this sector shows that wage restraint could be the *casus belli* for major turmoil in the near future. Massive bankruptcies are expected while whole industrial areas face a danger of lock-out. Vulnerable groups, such as the disabled and children, will grow in numbers.

Public policy is starting to address the issue of poverty. Both minimal wage and pension benefits are guaranteed to equal 35 per cent of the projected average wage in the same quarter, although this corresponds to a meagre 35 or 40 dollars a month, which, in many cases, does not ensure minimum basic needs. Nevertheless, the authorities are trying to build a social safety net, and, even if belated, financial resources and manpower are being increased and a more active labour policy is being implemented.

In addition, new actors such as local governments, local communities, NGOs, the Church, schools and family groups are entering the field of social assistance, while more emphasis on the needs of children, women and other vulnerable groups should be ensured by a newly created 'social council' as part of the cabinet.

The burden of preserving standards of living and social consensus will fall heavily on social assistance. Even if its budget was increased in 1990 and 1991, this does seem to be a high-risk strategy as still limited resources and an untested social assistance structure may not be able to catch the social fall-out. A stronger element of solidarity and redistribution in social policy would be desirable and necessary for future growth.

"Solidarity today, success tomorrow" was the popular slogan for the last ten years. But it seems that the social solidarity principle could be the first victim on the road to the long-awaited economic success.

The road from red to white (the Polish national colours) will not be rosy.

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This work examines the (initial) changes in social policies and the establishment of safety nets which have accompanied the transition to the market economy in Central and Eastern Europe. While strong emphasis has been placed so far on the necessary and welcome economic changes undertaken, to date, it appears that social policies have not received adequate attention. This neglect is even more worrisome as there are indications that the implementation of the economic reforms is encountering more difficulties than originally envisaged. Consequently, undesirable effects may result which could not only reduce the welfare of children and other population groups involved but also delay or reduce the overall effects of the new reforms. In *Children and the Transition to the Market Economy* special recommendations are made and greater emphasis is placed on Safety Nets and Social Policy which will benefit children and families, particularly those most at risk.

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